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In the Supreme Court of the United States

OCTOBER TERM, 1969

No. ——

FEDERAL TRADE COMMISSION, PETITIONER

v.

COLUMBIA BROADCASTING SYSTEM, INC., AND COLUMBIA RECORD CLUB, INC.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The Solicitor General, on behalf of the Federal Trade Commission, petitions for a writ of certiorari to review that portion of the judgment of the United States Court of Appeals for the Seventh Circuit entered in this case on July 18, 1969, that reversed part of the Commission's order and remanded to the agency for further proceedings.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, pp. 1a–17a) is not yet reported. The findings, conclusions, order and opinion of the Federal Trade Commission (App. D, *infra*, pp. 21a–94a; R. 482–556)[1] are not yet reported.

[1] "R." refers to the Joint Appendix filed in the court below.

JURISDICTION

The judgment of the court of appeals was entered on July 18, 1969 (App. C, *infra*, pp. 19a–20a [2]). By orders entered on September 23, 1969, and October 20, 1969, Mr. Justice Marshall extended the time for filing a petition for a writ of certiorari to and including November 14, 1969. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the court of appeals improperly reversed an order of the Federal Trade Commission prohibiting respondents from engaging in unfair methods of competition and remanded the case to the Commission to take additional evidence and reconsider its decision, on the basis of respondent's allegations, made for the first time in the appellate court, that after the record had been closed there had been significant changes in the competitive structure of the industry.

2. Whether the Commission properly concluded that respondents' exclusive dealing arrangements with record manufacturers constitute unfair methods of competition, in violation of Section 5 of the Federal Trade Commission Act.

STATUTE INVOLVED

Section 5(a) of the Federal Trade Commission Act, 38 Stat. 717, 719, as amended, 15 U.S.C. 45(a), provides in part:

[2] An earlier order of the court of appeals, which the court did not intend to be its judgment, was entered on June 26, 1969 (App. B. *infra*, p. 18a).

(1) Unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce, are declared unlawful.

* * * * * *

(6) The Commission is empowered and directed to prevent persons, partnerships or corporations * * * from using unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce.

STATEMENT

1. *The Commission proceedings.* On June 25, 1962, the Federal Trade Commission issued a complaint charging that Columbia Broadcasting System, Inc., and its wholly owned subsidiary, Columbia Record Club, Inc. (sometimes collectively referred to as "Columbia"), had engaged in unfair methods of competition, in violation of Section 5 of the Federal Trade Commission Act (R. 1–24). Insofar as here relevant, the complaint alleged (R. 9–10) that Columbia had foreclosed actual and potential competition in the record mail order market through licensing arrangements with nine independent record manufacturers which gave Columbia the exclusive right to distribute the licensor's records by direct mail subscription, *i.e.*, the "record club" method of distribution.[3]

[3] The complaint also alleged (R. 15–18) that Columbia (1) had fixed the prices to be paid to recording artists by the record manufacturers with which it had exclusive dealing arrangements and (2) had engaged in other illegal practices in the phonograph record industry, including additional price fixing, monopolization and attempted monopolization. The Commission held that Columbia had engaged in price fixing relating to recording artists, and the court of appeals upheld the

After lengthy administrative hearings, at which 11,000 pages of testimony were taken and 1400 exhibits (R. 31) were introduced—the evidence related principally to the period 1960–1961—the hearing examiner dismissed the complaint (R. 30–423). On appeal by complaint counsel, the Commission held that Columbia's exclusive licensing arrangements constituted unfair methods of competition (R. 533–534).[4]

2. *The Commission's findings.* The pertinent findings of the Commission can be summarized as follows:

Phonograph records are manufactured from original recordings or duplicates known as "masters" (R. 539, n. 6). They are distributed through wholesalers who buy the records from the manufacturers and sell them to retailers (R. 538), and through integrated sales systems of the manufacturers. One of the methods of distribution is the subscription mail or "record club" system (R. 540–541), under which the consumer joins the selling organization and agrees to purchase by mail a minimum number of records during a given period (R. 484).

The entire record market is highly concentrated. In 1960 the three largest producers, who are vertically integrated (Columbia, RCA and Capitol, the so-called "Big Three"), had 48 percent of total record sales of

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portion of its order directed against that practice (App. A, *infra*, pp. 14a–15a). The Commission, however, held that Columbia had not engaged in the second category of violations (R. 513, n. 70, 539, n. 5).

[4] The examiner's decision was rendered on September 30, 1964 (R. 423). The Commission heard oral argument on May 18, 1965 (R. xix), and rendered its decision on July 25, 1967 (R. 556).

$521 million, and Columbia's share of this figure was 21 percent (R. 497–498). In that year the Big Three had 90.6 percent of record club sales, and Columbia's portion was 56 percent [5] (R. 500).

Columbia adopted the club method in 1955 to prevent non-record firms from entering the mail-order market (R. 487). For three years the Club sold only Columbia label records, but in 1958 it concluded that it would be more profitable also to sell records produced by competing manufacturers (R. 487). Between May 1958 and December 1961, it entered into a series of licensing agreements with nine independent record manufacturers (R. 491–493, 515). The agreements were of one to three years duration, but in practice were regularly renewed (R. 493, n. 26). They gave Columbia the right to manufacture records from the licensors' "masters" for distribution through the Club (R. 491–493; 539);[6] the right was exclusive because the manufacturers agreed not to sell any of their records by the subscription or mail-order method, either directly or through sales to third persons for club or mail-order resale (R. 539). In return, Co-

[5] All of the records sold by the clubs are long-playing ("LP"), the only kind which can economically be distributed in this way (R. 504). In 1961, 75 percent of all records sold were LP; Columbia had 25 percent and the Big Three together had 56.5 percent of the LP market (R. 499).

[6] The nine licensors were: Caedmon Records, Inc.; Cameo-Parkway Records, Inc.; Kapp Records, Inc.; Liberty Records, Inc.; Mercury Records Corp.; Warner Bros.; United Artists Records, Inc.; Vanguard Recording Society; and Verve Records, Inc. (R. 525). The Warner Brothers and Vanguard contracts covered certain named records and the Vanguard contract was non-exclusive; the other seven contracts covered the licensor's entire catalog (R. 525).

lumbia guaranteed to sell a certain number of the licensors' records (R. 549). In entering into these arrangements, Columbia intended both to increase its market share and to prevent the licensors themselves from entering the club field or from selling their records to anyone else who might do so (R. 490).

Under its exclusive licensing arrangement, Columbia's unit cost to produce its licensors' records is 87.5 cents (R. 510, 519). Persons seeking those records for the purpose of entering the club market, however, must purchase them from wholesalers at prices ranging from $1.60 to $2.47 per record (R. 513–514).[7] Thus Columbia has a cost advantage of at least 72.5 cents ($1.60 minus 87.5 cents) over potential entrants in obtaining records (R. 514). This cost difference is a substantial barrier to entering the record club business (R. 519–520), since profit margins there, based on Columbia's experience, range between 24 and 75 cents per record (R. 514).

3. *The Commission's decision.* Holding that the record club business is an appropriate "line of commerce" within which to measure the anticompetitive effect of Columbia's exclusive licensing arrangements (R. 504–512, 532, 540–541), the Commission found that Columbia's cost advantage resulting from the lower prices it obtained under those arrangements "constitutes a serious impediment to entry into the club market, and the cause of a substantial lessening and prevention of competition within that market"

[7] There was evidence that the Big Three did not supply competing clubs (R. 522).

(R. 531–532).[8] As it explained in its conclusion No. 4 (R. 533–534),

> the existence of these exclusive grants to Columbia forces other clubs desiring to sell the records of those nine producers to go to the latters' wholesalers and pay $1.60 or more per record—as contrasted with the 87.5¢ the same records (Mercury, Kapp, Warner Bros., etc.) cost the Columbia Record Club. This cost disadvantage has the effect of barring potential newcomers that would otherwise have found the operation of a club profitable and hence of preventing competition with the clubs of the "big three" that could have otherwise been reasonably expected to flourish.

The Commission pointed out that the Big Three controlled and could bar other competitors from 48 percent of all records (R. 545); that Columbia's exclusive dealing arrangement "dries up" a significant share of the remaining records that otherwise would be available to competing record clubs—in 1961 Columbia's licensors had 11.2 percent of all LP's sold through retailer dealer stores (R. 546); that the actual anticompetitive effect of the exclusive dealing arrangements upon other record clubs was even greater than these figures indicate, since the "bulk of the records *suitable for club use* are apparently drawn in actual practice" from the relatively small group of records that become "hits," particularly from the 150 records that at any time are on the popularity "charts" published by the trade magazines (R. 546,

[8] The Commission rejected Columbia's business justifications for its exclusive licensing arrangements (R. 549–554).

emphasis in original); and that since in March 1962 the Columbia licensors had 22 percent of such hits (33[9] out of 150) (R. 517), "[t]hese licensing contracts foreclosed to potential club entrants (except on disadvantageous terms) some 41.2% of what would otherwise have been an 'open' market in 'hit' records suitable for club use" (R. 547, footnote omitted).

The Commission stated (R. 520) that the adverse effect of these arrangements upon potential competitors was illustrated by the unsuccessful attempt of the Diners Record Club to enter the record club business in 1958. According to the testimony of the president of that firm, the principal reason for its failure was

> a lack of adequate source of material of records to feature in the club. We had a basic repertoire from a number of companies, but we needed three major companies, certainly; Columbia, RCA, Capitol, *as well as the affiliated* [*licensor*] *companies to Columbia Record Club in order to successfully operate the business* [R. 523, emphasis added, brackets in original, footnote omitted].

The Commission found (R. 530) that, "as far as this trial record indicates," there has been "no successful entry into the 'club' market" other than the Big Three. The Commission noted reports in the trade press that the Record Club of America had entered the market; but it stated that since both Columbia and complaint counsel had opposed a recent motion by that firm to intervene (which motion was denied),

[9] As to four of the 33 records, however, Columbia did not have exclusive rights (CX 200; R. 517, n. 78).

it "assume[d] they are agreed that this new entrant, Record Club of America, has no competitive significance in the club market" (R. 530–531, n. 111).

As noted, the Commission found (R. 490) that one purpose Columbia had in entering into the exclusive licensing arrangements with the nine manufacturers was "to prevent those competitors from entering the club field on their own * * *" (R. 490). The Commission pointed out that in 1961 the sales of records of the nine Columbia licensors made by the Columbia Record Club were $12.8 million and constituted 16.3 percent of total record club sales; that since Columbia's sales in that year of $28.7 million of its own records was 36.7 percent of total record club sales, the effect of this combination by Columbia "with nine of its competitors" was to give it 53 percent of all club sales in a market in which the Big Three had more than 90 percent (R. 547–548); and that such an increase in an already highly concentrated market violated the standards this Court has applied in recent merger cases (R. 547–548).

4. *The court of appeals' decision.* A divided court of appeals set aside the portion of the Commission's order directed against the exclusive dealing arrangements, and remanded the case to the agency for further proceedings. The court upheld the Commission's findings that the record club market was an appropriate line of commerce within which to measure the effect of the arrangements upon competition (App. A, *infra,* pp. 6a–10a, 14a) and its findings as to the extent of market foreclosure the arrangements

caused.[10] It ruled, however, that although it "agree[d] with the Commission that Columbia's licensing agreements have foreclosed a share of the market, we feel that the Commission has failed sufficiently to examine the market structure" (*id.*, pp. 13a–14a). It stated that "the record club market * * * has undergone a significant change since the hearing examiner completed his hearings and entered his findings," because since 1963 (1) at least four new firms have entered the market, one of which (Record Club of America) "now claims to be the second largest record club in the industry"; (2) many "new 'hit' recording stars have cut their records on the labels of small manufacturers"; and (3) consumer tastes "have undergone a substantial change and with this, the entire record industry" (*id.*, p. 14a). The court concluded (*ibid.*) that

> because of the long delay in deciding this case and the substantial allegations of changes in the structure of the entire industry, and especially the club market, this case must be remanded to the Commission for further evidence as to the present structure of the record club market in order to determine whether supplies of records have been foreclosed from other clubs and whether such foreclosure has significantly prevented new entrants into the market.

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[10] The court stated (App. A, *infra*, p. 11a, footnote omitted):

"* * * the effect of the exclusive licensing agreement is to foreclose a competitor or prospective competitor of the Club from a segment of the total record manufacturing market which would otherwise be open to him. The Big Three account for 48% of the total record sales and Columbia's licensors represent another 11.1% of this market. Together, almost 60% of the record sales market is foreclosed from new club entrants."

Judge Kiley, dissenting, noted that "[t]he court agrees that the Commission properly decided that at that time [1960 and 1961] there was a violation of Sec. 5 of the Act" (*id.*, p. 16a), and stated (*id.*, 17a):

> I think that if there are changes in the market which render the Commission's order unrealistic vis-a-vis the market after 1962, and changed circumstances require modification of the order, the appropriate procedure is to affirm it, as I think the court should do. If petitioners thereafter wish to achieve a modification, they should have the burden of showing before the Commission that justice requires modification in view of the changed market conditions. The Commission has the power to modify the order under that procedure should it decide to do so.

REASONS FOR GRANTING THE WRIT

1. In reversing the portion of the Commission's order directed against Columbia's exclusive dealing arrangements and remanding the case for the agency to take evidence "as to the present structure of the record club market", the court of appeals departed from settled principles governing the authority of reviewing courts to require reopening of administrative records to take account of changed conditions. In *Interstate Commerce Commission* v. *Jersey City*, 322 U.S. 503, in holding that the Commission had not abused its discretion in refusing to reopen a rate case because of a claim by the Price Administrator that the record was "stale" (p. 514), this Court explained why the reopening of administrative records for al-

leged staleness was within the sound discretion of the agency and not for the courts (pp. 514–515):

> One of the grounds of resistance to administrative orders throughout federal experience with the administrative process has been the claims of private litigants to be entitled to rehearings to bring the record up to date and meanwhile to stall the enforcement of the administrative order. Administrative consideration of evidence—particularly where the evidence is taken by an examiner, his report submitted to the parties, and a hearing held on their exceptions to it—always creates a gap between the time the record is closed and the time the administrative decision is promulgated. This is especially true if the issues are difficult, the evidence intricate, and the consideration of the case deliberate and careful. If upon the coming down of the order litigants might demand rehearings as a matter of law because some new circumstance has arisen, some new trend has been observed, or some new fact discovered, there would be little hope that the administrative process could ever be consummated in an order that would not be subject to reopening. It has been almost a rule of necessity that rehearings were not matters of right, but were pleas to discretion. And likewise it has been considered that the discretion to be invoked was that of the body making the order, and not that of a reviewing body.

The Court in *Jersey City* reviewed the numerous decisions in which it had upheld agency refusals to reopen records, and pointed out that "Only once in the history of administrative law has this Court

reversed a Commission for refusing to grant a rehearing on the contention that the record was 'stale'" (p. 515). In that case, *Atchison, T. & S.F. R. Co.* v. *United States,* 284 U.S. 248, 260–262, the Court held that the Commission had improperly refused in 1931 to reopen a record in a rate case that had been closed in 1928 (the order not yet having become effective); the ground of decision was that the facts developed in 1928 were no longer viable under the drastically changed economy that existed in the depth of the depression. In the *Jersey City* case this Court pointed out (322 U.S. at 515) that *Atchison* was "promptly restricted * * * to its special facts * * * and it stands virtually alone." This Court recently applied the same principle in refusing to require the Interstate Commerce Commission to hold a new hearing to consider evidence of "present conditions" relating to the construction of new track; the fact that the case had been pending for 10 years, the Court stated, "rather than being a reason for holding additional hearings, operates to the contrary." *Illinois C.R. Co.* v. *Norfolk & W. R. Co.,* 385 U.S. 57, 75.

Under the foregoing principles, the decision whether to reopen the record is for the discretion of the agency. Only in the exceptional case where the agency has abused its discretion will the courts interfere. *A fortiori,* the courts should not direct an agency to reopen an allegedly stale record when the claim has not even been presented to the agency and there are no extenuating circumstances to justify such refusal. Cf. *United States* v. *Tucker Truck Lines,* 344 U.S. 33.

This is precisely such a case. At no time during the Commission proceedings did Columbia ask the agency to reopen the record to receive evidence of changed conditions in the industry. Columbia was aware of the size of Record Club of America before the Commission decided the case. In February 1967, five months before the decision, Columbia filed an opposition to Record Club of America's application to intervene in the Commission proceedings; in that application the president of Record Club stated that in 1966 it had more than 700,000 members and sales of $8 million (R. 468, 472–477). Columbia did not even file a petition for rehearing with the Commission urging it to reopen the record because of alleged staleness. Instead, it waited until the case was in the court of appeals to raise the claim.

In such circumstances, the proper procedure is that indicated by Judge Kiley in his dissent: the court, having upheld the Commission's determination of violation on the record as made, should have upheld its orders; "[i]f petitioners thereafter wish to achieve a modification, they should have the burden of showing before the Commission that justice requires modification in view of the changed market conditions" (App. A, *infra*, p. 17a). See 16 C.F.R. 3.71, 3.72(b)(2). The court's disposition of the case, however, gives new life to the practice condemned in *Jersey City, supra,* 322 U.S. at 514, by which litigants claim "to be entitled to rehearings to bring the record up to date and meanwhile to stall the enforcement of the administrative order."

The decision of the court of appeals, if allowed to

stand, portends particularly serious problems for the Federal Trade Commission. That agency conducts many lengthy proceedings in which it must make expert judgments as to the probable effects of various restrictive acts and practices in different segments of the economy. The nature of the Commission's determination in such cases compels it to develop detailed evidence with respect to the industry involved—a process that is protracted and in which the evidence can never be completely current. The market in which the anticompetitive effects are likely to be felt is not a static institution; rather, it usually is a dynamic organism in a constant state of flux in which the challenged practices themselves may have a significant impact upon its structure. The statutes that the Commission administers frequently require it to stop anticompetitive practices in their incipiency, before they have developed into full-blow violations of the antitrust laws. See *Federal Trade Commission* v. *Brown Shoe Corp.*, 384 U.S. 316. The only way in which the Commission efficiently and effectively can perform its function in such cases is on the basis of the most recent evidence available at the time of the hearing that provides an adequate basis for its expert economic judgments. It cannot fairly be asked—or expected—to keep updating the record to reflect more recent changes in market structure that do not undermine the soundness of its basic long-range economic predictions and judgments.

Since the validity of Commission cease-and-desist orders in such cases does not depend upon a determi-

nation of the present effect of the practices involved but upon a judgment as to their probable future effect if allowed to continue and develop, the present case differs significantly from *American Committee for Protection of Foreign Born* v. *Subversive Activities Control Board,* 380 U.S. 503, and *Veterans of the Abraham Lincoln Brigade* v. *Subversive Activities Control Board,* 380 U.S. 513. In those cases the Subversive Activities Control Board had ordered two organizations to register as Communist-front organizations. The Court held that under the statute "reasonably current [Communist Party] aid and control must be established to justify a registration order" (380 U.S. at 505), and that because of the staleness of the evidence and significant changes that had occurred after the record was closed—in one case the individual upon whose Communist Party activities the Board had heavily relied had died—"the record should be brought up to date to take account of supervening events" (pp. 504–505). The Court also was of the view that the records as they then stood did not provide an appropriate basis for deciding the serious constitutional issues that had been raised. 380 U.S. at 505; 380 U.S. 513–514. In the present case, on the other hand, there is no constitutional issue and the kind of determination necessary to support the Commission's cease-and-desist order involves quite

different considerations than those involved in the Board's registration order.[11]

2. If, contrary to our submission and the views of dissenting Judge Kiley below, the court of appeals decision rests in part upon the court's rejection of the Commission's theory of violation, then that ruling, too, is erroneous and warrants review. As set forth in the Statement, the Commission found that Columbia's exclusive licensing arrangements cut off a substantial and important source of records to potential competitors in the club market. The Commission properly concluded that such fencing out of competitors constitutes an unfair method of competition, in violation of Section 5 of the Federal Trade Commission Act. *Federal Trade Commission* v. *Brown Shoe Corp.*, 384 U.S. 316; *Atlantic Refining Co.* v. *Federal Trade Commission*, 381 U.S. 357.

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[11] Cases in which the Federal Communications Commission based its decision awarding a radio or television station license in large measure upon the persons connected with the successful applicant, and such persons terminated their connection with the applicant after the record was closed, are similarly distinguishable. In such cases the reviewing court justifiably remanded to the agency to reconsider in the light of such change. See *Fleming* v. *Federal Communications Commission*, 225 F. 2d 523 (C.A.D.C.); *Southland Television Co.* v. *Federal Communications Commission*, 266 F. 2d 686 (C.A.D.C.). See also, *WORZ, Inc.* v. *Federal Communications Commission*, 345 F. 2d 85 (C.A.D.C.), certiorari denied *sub nom. Mid-Florida Television Corp.* v. *Federal Communications Commission*, 382 U.S. 893 (change in character of community to be served).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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NOVEMBER 1969.

APPENDIX A

FEDERAL TRADE COMMISSION DOCKET 8512

In the United States Court of Appeals for the Seventh Circuit

September Term, 1968—April Session, 1969

No. 16492

COLUMBIA BROADCASTING SYSTEM, INC., AND COLUMBIA RECORD CLUB, INC., PETITIONERS

v.

FEDERAL TRADE COMMISSION, RESPONDENT

APPEAL FROM AN ORDER OF THE FEDERAL TRADE COMMISSION

June 26, 1969

Before KNOCH, *Senior Circuit Judge,* and KILEY and KERNER, *Circuit Judges.*

KERNER, *Circuit Judge.* The Federal Trade Commission issued a complaint on June 25, 1962, against Columbia Broadcasting System, Inc. (CBS) charging CBS and its subsidiary, Columbia Record Club, Inc. (Club) with violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45.[1] Hearings were held and the hearing examiner entered an order on September 30, 1964, dismissing the complaint. On July 25, 1967, the Commission, Commissioner Elman not

[1] Section 5(a)(1): Unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce are hereby declared unlawful (15 U.S.C. 45(a)(1)).

concurring, reversed the examiner's findings and from this decision CBS appeals.

Columbia Broadcasting System, Inc. is a corporation organized under the laws of New York with its principal place of business in New York City. One of its operating divisions, Columbia Records (Columbia), manufactures and sells phonographic records. In 1961 this division produced 20% of CBS' total sales.

Total sales in the record industry were $521 million in 1960. Columbia Records, the leading producer and seller, accounted for 21% of the industry's total sales. The "Big Three" record manufacturers, Columbia. R.C.A. and Capitol, produced 48% of total sales. Most of the records sold are LPs (long playing) and singles: in 1961 the breakdown in dollar volume was LPs. 75%; singles, 24%; and EPs (extended play) 1%. Columbia's share of LP sales was 25.4% while the Big Three together, shared 56.5% of the LP market.

Columbia has two main channels of record distribution: 1) the records are sold to distributors, either Columbia owned or independent, who sell them to subdistributors and independent retailers; or 2) the records are sold directly by the Columbia Record Club to the consumer through the use of a "subscription" form of mail order business. In 1961 and 1962, Club sales were 50% of Columbia's total record dollar sales.

Columbia entered the mail order subscription sale of records by forming the Columbia Record Club in 1955 in response to a threat of competition from other companies. The Club's method of mail order sale was to induce the consumer to join the Club and agree to purchase a minimum number of records during the year by offering a certain number of records at below cost prices. For example, in 1963, the Club's offer consisted of six records for an aggregate price of

$1.89 plus 55¢ postage provided the new member agreed to buy another six records in the next twelve months at the list price of $3.98 each plus 35¢ postage per record. In the second year of membership, for every two records a member purchased, he received one free. The first year the member paid an average of $2.37 per record and in the second year the average price was $2.88 per record.

From 1955–58, the Club only sold Columbia records. However, in 1958, the Club decided to sell records of competitors. To acquire a more diversified catalog, the Club entered into licensing agreements with some of the small record manufacturers.[2] The agreements had a duration of from one to three years with options to renew. Columbia guaranteed the sale of a certain number of records in return for an agreement by the licensor not to sell any of its catalog to another club. The licensor could still sell to wholesalers who could in turn sell to other clubs or retailers.

The licensing agreements also provided that the licensors should make every effort to reduce royalties paid to artists on records sold through the Club.

[2] See following table:

Licensor Record Manufacturer	Date of Contract	Licensor's Share of Retail Dealer Sales in Year Prior to Contract	
		As a % of Total Record Dollar Sales	As a % of Total LP Dollar Sales
1. Caedmon	5/15/58		
2. Verve	3/31/59	0.6	1.1
3. Mercury	4/1/60	3.5	2.7
4. Warner Brothers	9/15/60	1.5	1.4
5. Kapp	10/7/60	1.7	1.8
6. Vanguard	6/1/61	*	1.5
7. United Artists	7/1/61	1.6	1.1
8. Liberty	10/25/61	1.7	1.0
9. Cameo-Parkway	12/15/61	1.2	0.7
Total		11.8	11.3

* Indicates less than 0.5%.

Columbia's practice was to pay an artist only 50% of his royalty on records sold by the Club and no royalty on free bonus records offered by the Club. The licensing agreements contained a provision requiring the licensor to follow the same policy wherever it was practicable. In certain contracts Columbia only agreed to be liable for royalties paid at these reduced rates and any royalty paid by the licensor above these rates was to be absorbed by the licensor.

In 1960, Columbia's share of record club sales was 56% while the Big Three together accounted for 90.6% of total sales through clubs. Columbia Club was the only club offering outside labels to its members. In 1961, Columbia's licensors accounted for 11% of total record sales. Of the 150 largest selling monaural LPs on March 24, 1962, 103 of these records were on Columbia, Columbia licensors, R.C.A. or Capitol labels. Columbia and its licensors, alone, accounted for 65 of the "hits" or 43.3%, while the licensors themselves had 33 of the records on the listing or 22%.

The total acquisition cost to the Club of a record produced under a licensing agreement was 87.5¢. The Club's cost of marketing these records, is $1.255 and when added to the acquisition cost, the total cost is $2.13.[3] The acquisition cost to a competitor, either

[3] See the following:

COSTS: Acquisition costs	*Amount*
Manufacturing cost	$0.428
Royalties to licensors	.178
Copyright royalties	.137
AFM fees [union fees]	.024
Excise tax	.108
Total	$.875
OTHER COSTS	
Free merchandise (brushes, racks, etc.) used in enrollment offers	.123
Advertising costs: includes magazine advertising; newspaper advertising; direct mail advertising (including postage); get a friend	

retailer or club, ranges from $1.60 to $2.47 for the same record. The average cost to Columbia retailers was $2.12 in 1961. The competitors' additional operating cost would raise their total cost above $2.13. In 1961, 30% of the records sold by the Club were produced under these licensing agreements.

While the number of companies that have entered the business of manufacturing records has grown substantially during the 1950s and early 1960s, the number of entries into the club market has been small. According to the evidence presented to the Commission, aside from the entry of R.C.A. and

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advertising; radio support, and other miscellaneous advertising expenditures to acquire new members for the Club	.353
Sales promotion: includes creating and printing of monthly magazines and special promotion magazines; postage to mail the magazines; postage to mail monthly statements of account to members; supply costs connected with the mailing of various materials to members	.172
Other operating and distribution expenses: includes operating and warehousing, payroll costs; allocated employment benefits, including pension expense, payroll taxes, compensation insurance, group insurance, hospitalization, stock purchase plan; leased equipment expense, primarily IBM electric accounting machines and computer equipment; facilities expenses, which includes rent, depreciation of owned buildings, power, heat, maintenance, guard service, personnel and purchasing; internal supplies used in the operation of the business which do not go to record club members, e.g.; approximately two hundred thousand IBM cards, computer tapes, pencils, papers, pens; other items including depreciation of furniture and owned equipment, meal allowances, travel and business meeting expenses, outside services, etc. Also included in these expenses are postage for shipping records to members as well as mailing cartons for shipping the records and depreciation for special-purpose packaging equipment	.289
Bad debts: includes the accounts written off to the Reserve for Bad Debts including commissions paid to external collection agencies on accounts turned over to them; accounts in the hands of collection agencies which had not been written off to the Reserve for Bad Debts, less estimated collections, after commissions, from the collection agencies; estimated additional bad debts to be turned over to collection agencies less a provision for collection of a percentage from such accounts by external collection agencies	.318
Total	2.13

Capitol after 1955, there have been no significant entries into the club business. However, after the examiner closed the hearings, Record Club of America, Longine, Dot and Starday have all entered the club business with the Record Club of America claiming to be the second largest club in the industry.[4]

The Commission, in reversing the hearing examiner, found that the exclusive licensing agreements violated Section 5 of the Federal Trade Commission Act in that the exclusive provision of the contract had the effect of barring new entrants into the record club market and that the artist royalty agreements constituted a form of price fixing which is also violative of Section 5. The Commission entered a cease and desist order prohibiting exclusive licensing agreements and agreements fixing artist royalty payments.

To determine whether the exclusive licensing provision is an unfair method of competition under Section 5 of the Federal Trade Commission Act, the relevant market within which to measure the effect on competition must be defined. The relevant product market is the area of effective competition. The area of effective competition depends on the degree of substitutability which may be measured by the cross-elasticity of demand. CBS argues that since all records are the same whether distributed through retail dealers or mail order sellers because artists record the same material on both LPs and singles, there is complete interchangeability and, therefore, the relevant market is the entire record market. However, the Supreme Court in *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 356–57 (1963), found

[4] On February 13, 1967, the Record Club of America petitioned to intervene in the proceedings under Section 3.9 of the Commission's Rule of Practice for Adjudicative Proceedings. Complaint counsel and CBS opposed intervention and the Commission denied the motion.

that commercial banking as compared to other forms of banking was a separate market even though other financial institutions offered the same services. In *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 325 (1962), the Supreme Court concluded that while

> The other boundaries of a product market are determined by the reasonable interchangeability of use . . . , within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. . . .
> The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors.

The Commission found that the record club market had "sufficient peculiar characteristics," *United States* v. *E. I. DuPont de Nemours & Co.,* 353 U.S. 586, 593 (1957), to make it a submarket. The Commission based its finding of a separate submarket on three factors: 1) Columbia by its own acts treated the club market as being separate; 2) differences in demand; and 3) differences in cost.

Columbia's recognition of a separate club market came in 1955. In that year, other mail order sellers from outside the record industry threatened to apply their distribution system to the sale of records. Fearful of competition, Columbia decided to plunge headlong into the newly formed club market. In 1958, Columbia, realizing that many members were being lost because of inability to supply a wide variety of records, entered into exclusive licensing agreements with other manufacturers. Concerned that these other manufacturers might compete with Columbia in the

club market, Columbia insisted on an exclusive provision in the licensing agreement which prevented these other manfacturers from selling to other clubs but did not prohibit them from selling to retailers. All of these corporate acts were directed at reducing competition in the club market and not in the industry as a whole. We agree with the Commission that Columbia itself through its actions has recognized the club form of distribution as a separate market in which to compete.

The Commission's characterization of the demand function in the club distribution channel is supported by substantial evidence. The Commission found that the demand function in the club market was different from the demand function in the record market as a whole. The characteristics of purchasers in the club market (members) are distinct. A club member is one who prefers to sit at home and select records rather than make many trips to the store; wants guidance in repertoire selection; seeks economical values; and is willing to accept the disadvantages of club membership such as long waiting periods for delivery, limited selection and a contractual commitment as to the number of purchases. While a record club member may purchase certain records from a dealer, the Commission's findings as to the special characteristics of a club member are not clearly erroneous.

Price differentiation is a factor in defining a submarket. See *United States* v. *Aluminum Corporation of America,* 377 U.S. 271 (1964). Here, price has more significance in the first year membership when the price of records purchased through the record club is $2.37 and the average price for records purchased through a dealer is $2.98. In the second year of membership, price drops out as an important factor since the price differential is only 10¢ per record and the

peculiar characteristics of the customer become more important in determining the boundaries of the submarket. See *Brown Shoe Co.* v. *United States*, 370 U.S. 294 (1962). The prices of the Club are in direct competition with the prices of other clubs, and since there is at least a six-month time lag from the date of the decision as to the final contents of the bonus offer until it appears in advertisements, price competition between retailers and clubs is minimal.

We agree with the finding that the club form of distribution is separate from other mail order sellers. The club form requires a contractual commitment and attracts members by the use of the bonus type of offer. In mail order selling there is no commitment to make further purchases and the music is usually of a very specialized nature. The characteristics of the customers who purchase from mail order sellers are different from those who buy through clubs.

We fail to find any real significance in the Commission's findings as to differences in cost structure. The Commission found that the cost structure of the Club is different. In acquiring records from licensors the Club pays 87.5¢ while another club would have to pay at least $1.60 to acquire the same record from a distributor. Evidence of the Club's advantage over other clubs is its willingness to commit itself to fulfilling substantial guarantees. However, such evidence would only support a finding that the Club enjoys a competitive advantage over other clubs and not that the clubs constitute a separate submarket.

The Commission also claimed that differences in cost between the Club and retailers was further evidence of separate markets. While the Club paid a licensor 87.5¢ for a record, a dealer had to pay at least $1.60 for the same recording. The Commission's finding that the Club pays less than a retailer for the

same record supports a conclusion as to the benefits of vertical integration but does not support a finding of separate markets.

We agree with the Commission in its application of the *Brown Shoe* test to the record industry. While all record sales constitute an industry-wide product market, within this market the record clubs constitute a "well-defined submarket."

The Commission found that the exclusive licensing agreements coupled with the fact that the Big Three record companies were integrated had the same effect as a horizontal merger between the Club and the licensors, and

> [F]alls squarely within the rule of *Philadelphia Nat'l Bank* against a consolidation that "produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market. . . ." *United States* v. *Philadelphia National Bank*, 374 U.S. 321, 363 (1963). Columbia Broadcasting System, Inc., FTC Dkt. No. 8512 (July 25, 1967) Slip Opinion p. 12.

The Commission, while alluding to the possible violation of Robinson-Patman standards, decided to rely strictly on merger law:

> Since the price differential (87.5¢ vs. $1.60) has allowed into the club market no significant competitors other than the integrated "big three" and has thus given the Columbia Record Club a virtual monopoly on the sale of the records of these nine firms through clubs, we think the situation should be evaluated primarily in terms of merger standards. *Id.* 11 n. 29.

CBS complains that the Commission's reliance on a per se horizontal merger standard is misplaced. Rather, the exclusive provision is ancillary to the licensing agreement and must be sustained if it is

reasonable. *United States* v. *Addyston Pipe and Steel Co.*, 85 Fed. 271 (6th Cir. 1898), affirmed, 175 U.S. 241 (1899). In *Packard Motor Car Co.* v. *Webster Motor Car Co.*, 243 F. 2d 418 (D.C. Cir. 1957), cert. denied, 355 U.S. 822 (1957), the court did not adopt a per se approach in upholding the validity of an exclusive dealership agreement initiated by the dealer, and CBS believes that the present case is on all fours with *Packard*. Too, CBS contends that since the "merger" is a short term contractual arrangement and not permanent, a different standard must be applied.

The characterization of the relation between Columbia and the licensors as a horizontal merger between the Club and the licensors is not in tune with the reality of the situation. Columbia, the manufacturer, and the licensors have entered into an agreement to supply the Club with outside labels. In this light, we categorize the relation as in the nature of a horizontal merger with the effects of a vertical merger. In the field of horizontal mergers the Supreme Court has been influenced by concentration and trends in concentration and has not concerned itself with ease of entry. Here, the effect of the exclusive licensing agreement is to foreclose a competitor or prospective competitor of the Club from a segment of the total record manufacturing market which would otherwise be open to him. The Big Three account for 48% of the total record sales and Columbia's licensors represent another 11.1% of this market. Together, almost 60% of the record sales market is foreclosed from new club entrants.[5] In this context, the problem here is different from that presented in *United States* v. *Columbia Pictures Corp.*, 189 F. Supp. 153 (S.D. N.Y., 1960), where there was no barrier to entry and the agree-

[5] The sales figures are a measure of production and the degree of market acceptance.

ment was viewed as a horizontal merger. Kessler and Stern, *Competition, Contract and Vertical Integration,* 69 Yale L.J. 1, 77 n. 353 (1959).

The Supreme Court in analyzing vertical mergers has looked to the extent of foreclosure and its relation to the structure of the market. In *Standard Oil Co.* v. *United States,* 337 U.S. 293 (1949), and *F.T.C.* v. *Motion Picture Advertising Serv. Co.,* 344 U.S. 392 (1953), the Court held that the standard of legality is determined by the degree of market foreclosure. However, in *Brown Shoe* v. *United States,* 370 U.S. 294 (1962), the Court said that "in cases . . . in which the foreclosure is neither of monopoly nor *de minimis* proportions, the percentage of the market foreclosed by the vertical arrangement cannot itself be decisive." 370 U.S. at 329. "Only a further examination of the particular market—its structure, history and probable future—can provide the appropriate setting for judging the probable anticompetitive effect of the merger." 370 U.S. at 332 n. 38.

CBS contends that while a portion of the market may be foreclosed from other record clubs, the effect on competition is minimal because of the short term nature of the agreement coupled with the overall market structure. CBS relies on *United States* v. *Philadelphia Nat'l Bank,* 374 U.S. 321 (1963), where the Court stated that "integration by merger is more suspect than integration by contract, because of the greater permanence of the former." 374 U.S. at 366. In *F.T.C.* v. *Motion Picture Advertising Serv. Co.* 344 U.S. 392 (1953), the Commission found that exclusive contracts of five years unreasonably restrained competition and that the company could not enter any agreements for longer than a year. In upholding the Commission's order, the Court said, "The precise impact of a particular practice on the trade is for the

Commission, not the courts, to determine. The point where a method of competition becomes 'unfair' within the meaning of the Act will often turn on the exigencies of a particular situation, trade practices, or the practical requirements of the business in question." 344 U.S. at 396. Columbia just like Motion Picture Advertising is entering into short term exclusive licensing contracts in order "to bolster horizontal power." Kessler and Stern, 69 Yale L.J. at 56, and we agree with the Commission that the short term nature of the agreements does not lessen their anti-competitive effect.

CBS relies heavily on Doubleday and Co., Inc., 50 F.T.C. 263 (1953). *Doubleday* involved licensing agreements between a publisher and a non-integrated book club whereby the book club was given an exclusive right to publish and sell "book club editions." Under the exclusive licensing agreement, a book club was able to offer the book at a substantially lower price than retailers. The complaint contended that the failure to grant the same rights to retailers as it gave to book clubs violated Section 5. The Commission held that the increased competition between retailers and book clubs that resulted from such agreements did not violate Section 5. Here, the situation is entirely different because we are concerned with competition between record clubs rather than competition between clubs and retailers. The exclusive agreements coupled with the fact that the large record manufacturing companies are integrated prevent other record clubs from forming and, thereby, reduce competition in the record club market. The *Doubleday* case is clearly distinguishable.

While we agree with the Commission that Columbia's licensing agreements have foreclosed a share of the market, we feel that the Commission has failed

sufficiently to examine the market structure. It is true that the record club market is the relevant market within which to measure the effect on competition. However, this market itself has undergone a significant change since the hearing examiner completed his hearings and entered his findings. Since 1963, there have been at least four new entrants into the record club market. One of these, the Record Club of America, now claims to be the second largest record club in the industry. The Commission's assumption that "the price differential . . . has allowed into the club market no significant competitors other than the integrated 'big three'", Columbia Broadcasting System, Inc., FTC Dkt. No. 8512 (July 25, 1967) Slip Opinion p. 11 n. 29., does not seem to be true. Too, the consumer tastes have undergone a substantial change and with this, the entire record industry. Many of the new "hit" recording stars have cut their records on the labels of small manufacturers. As a result, the size and nature of the foreclosure may have changed. The Commission's investigation of Columbia's practices began in 1959 and the complaint was filed in 1962. Much of the evidence in the record pertains to the years 1960 and 1961. The Commission did not hand down its opinion until July of 1967. We are of the opinion that because of the long delay in deciding this case and the substantial allegations of changes in the structure of the entire industry, and especially the club market, this case must be remanded to the Commission for further evidence as to the present structure of the record club market in order to determine whether supplies of records have been foreclosed from other clubs and whether such foreclosure has significantly prevented new entrants into the market.

CBS also attacks that portion of the cease and desist order which is directed at the fixing of artist

royalties. CBS claims that since provisions fixing royalties have been deleted from all contracts, the Commission may not enter a cease and desist order. It is fundamental to the powers of the Commission that it have wide discretion in implementing its decisions. We do not think that the use of a cease and desist order in this situation was an abuse of discretion. *Spiegel, Inc.* v. *F.T.C.*, — F. 2d — (7th Cir. No. 17210, June 11, 1969).

CBS contends that Commissioner MacIntyre should have disqualified himself from participation in this case because of Commissioner MacIntyre's involvement in the *Doubleday* litigation, 50 F.T.C. 263 (1953), when he was a staff member of the Commission. The Administrative Procedure Act provides:

> An employee or agent engaged in the performance of investigative or prosecuting functions for an agency in a case may not, in that or a factually related case, participate or advise in the decision. 5 U.S.C. § 554(d).

It will be remembered that *Doubleday* involved agreements between a publisher and a book club in which a book club was given the exclusive right to publish and sell "book club editions." The fact that *Doubleday* involves book clubs and this case involves record clubs does not make the two "factually related" as this phrase is used in the A.P.A. Too, we do not believe MacIntyre's participation violated due process.

We reverse and remand this case to the Commission for further proceedings as to the structure of the record club market consistent with this opinion. In all other matters, we affirm.

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED.

No. 16492

KILEY, *Circuit Judge,* dissenting.

I dissent from the court's judgment. The court's opinion approves the Commission's determination of the relevant market, a record club market separate from the general record market. It also approves the finding that the exclusive license agreements effectively foreclose a prospective competitor from a market otherwise open to him, and decides that the short terms of the agreements do not lessen their anti-competitive effect. But the court's judgment nevertheless sets the Commission's order aside. The essential reason given is that the Commission's order is stale. In the court's view, significant and substantial changes have taken place in the market since the hearing examiner completed his hearings and entered his findings, and further evidence is needed because the Commissioner did not sufficiently examine the market structure and at least four new entrants have come into the market since 1963, including the Record Club of America which claims to be the second largest club in the industry.

I am afraid that by the time the market structure is sufficiently examined, further evidence gathered, complaint amended, hearing examiner's decision filed and the Commission's order entered, several years from now, the market will probably have undergone further significant and substantial changes. A petition for review filed then will speak again of an order unrelated to conditions of the current market.

The Commission's decision covered petitioner's practices principally in 1960 and 1961. The court agrees that the Commission properly decided that at that time there was a violation of Sec. 5 of the Act. It is unfortunate of course that in this area there is a perplexing time lag between complaint and order.

But the record consists of more than 11,000 pages of testimony and over 1,400 exhibits. A similar perplexity arises for the same reason in anti-trust cases where large companies and a large government are contestants. The situation does not seem to improve as time goes on, but rather to grow worse. The indication seems to be that the evils of the delays inhere in the nature of our legal system and economy, and are "fleas that come with the dog."

I think that if there are changes in the market which render the Commission's order unrealistic vis-a-vis the market after 1962, and changed circumstances require modification of the order, the appropriate procedure is to affirm it, as I think the court should do. If petitioners thereafter wish to achieve a modification, they should have the burden of showing before the Commission that justice requires modification in view of the changed market conditions. The Commission has the power to modify the order under that procedure should it decide to do so. See 15 U.S.C. § 45(b); *American Chain & Cable Co.* v. *FTC*, 142 F. 2d 909 (4th Cir. 1944). See also *Mine Workers* v. *Eagle-Picher Co.*, 325 U.S. 335, 342, where *American Chain* is discussed with approval.

I would affirm the Commission's order.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit.

APPENDIX B

United States Court of Appeals for the Seventh Circuit Chicago, Illinois 60604

Thursday, June 26, 1969

Before

Hon. WIN G. KNOCH, *Senior Circuit Judge*
Hon. ROGER J. KILEY, *Circuit Judge*
Hon. OTTO KERNER, *Circuit Judge*

No. 16492

COLUMBIA BROADCASTING SYSTEM, INC., AND COLUMBIA RECORD CLUB, INC., PETITIONERS

v.

FEDERAL TRADE COMMISSION, RESPONDENT

PETITION FOR REVIEW OF AN ORDER OF THE FEDERAL TRADE COMMISSION

This cause came on to be heard on the petition for review of an order of the Federal Trade Commission entered on July 25, 1967, and the record from the Federal Trade Commission, and was argued by counsel.

On consideration whereof, it is ordered by this Court that the said order of the Federal Trade Commission be, and the same is hereby AFFIRMED in part, REVERSED in part, and that this cause be, and it is hereby REMANDED to the Federal Trade Commission for further proceedings, in accordance with the opinion of this Court filed this day. Upon presentation, an appropriate judgment will be entered.

APPENDIX C

In the United States Court of Appeals for the Seventh Circuit

No. 16,492

COLUMBIA BROADCASTING SYSTEM, INC., AND COLUMBIA RECORD CLUB, INC., PETITIONERS

v.

FEDERAL TRADE COMMISSION, RESPONDENT

JUDGMENT

Petitioners, having filed in this Court on October 6, 1967, a petition to review and set aside an order to cease and desist issued against them on July 25, 1967, by the Federal Trade Commission, respondent herein, and this Court on June 26, 1969, having rendered its decision whereby it affirmed in part and reversed in part said order to cease and desist, and remanded the cause to the Federal Trade Commission for further proceedings in accordance with the opinion of the Court filed on June 26, 1969;

NOW, THEREFORE, IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the following part of said order to cease and desist is affirmed and enforced:

> IT IS ORDERED that respondents Columbia Broadcasting System, Inc., and Columbia Record Club, Inc., and their officers, representatives, agents and employees, successors, or assigns, directly or indirectly, or through any corporate or other device, in connection with the manufacture, promotion, offering for sale, sale and distribution of phonograph records in com-

merce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

Entering into, maintaining, or continuing any contract, licensing agreement, or understanding with any other manufacturer or producer of phonograph records to:

Establish, fix, or maintain the price or royalty paid by any other manufacturer or producer of phonograph records to any artist for such artist's recording services.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that petitioners are commanded to obey and comply with that part of the Commission's order which is hereby affirmed and enforced;

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that the remainder of said order to cease and desist is reversed and that this cause be and it is hereby remanded to the Federal Trade Commission for further proceedings, in accordance with the opinion of this Court filed on June 26, 1969.

By the Court.

WIN G. KNOCH,
United States Circuit Judge.
OTTO KERNER,
United States Circuit Judge.

I join in the court's judgment only in so far as it affirms and enforces the Commissioner's Order,

ROGER J. KILEY,
United States Circuit Judge.

A true copy.
Teste:

KENNETH J. CARRICK,
Clerk of the United States Court of Appeals,
for the Seventh Circuit.
By H. K. MCCORMACK,
Deputy Clerk.

APPENDIX D

United States of America Before Federal Trade Commission

Commissioners:

Paul Rand Dixon, Chairman
Philip Elman
Everette MacIntyre
John R. Reilly
Mary Gardiner Jones

Docket No. 8512

IN THE MATTER OF COLUMBIA BROADCASTING SYSTEM, INC., A CORPORATION, AND COLUMBIA RECORD CLUB, INC., A CORPORATION

FINDINGS AS TO THE FACTS, CONCLUSIONS AND ORDER

The Federal Trade Commission issued its complaint in this matter on June 25, 1962, charging that the Columbia Broadcasting System, Inc., and its wholly owned subsidiary, Columbia Record Club, Inc., has engaged in certain unfair business practices in violation of section 5 of the Federal Trade Commission Act, 15 U.S.C. 45. Hearings were held before a hearing examiner of the Commission, and testimony and other evidence in support of and in opposition to the allegations of the complaint were received into the record. In an initial decision filed September 30, 1964, the examiner found that said charges of law violation were not sustained by the evidence and ordered the dismissal of the proceeding.

The Commission, having considered the appeal filed by counsel supporting the complaint and the entire record, and having determined that the initial decision should be vacated and set aside, now makes these its findings as to the facts, conclusions drawn therefrom, and order, the same to be in lieu of those contained in said initial decision.

FINDINGS AS TO THE FACTS

1. The respondent, Columbia Broadcasting System, Inc. (hereinafter CBS or Columbia) is a corporation organized and existing under the laws of the State of New York, with its principal office and place of business at 485 Madison Avenue, New York, New York. It has seven operating divisions: (a) CBS Television Network, (b) CBS Television Stations, (c) CBS Radio, (d) CBS Laboratories, (e) CBS International, (f) Columbia Records, and (g) CBS News. Its aggregate sales increased from $316.5 million in 1955 to $473.8 million in 1961.[1] Its total net assets increased, in that same period, from $74.0 million to $142.4 million.

2. An unincorporated division, Columbia Records Division, produces phonograph records in its four (4) manufacturing plants[2] and sells them to a wholly owned subsidiary, Columbia Records Division Corporation, which in turn sells to (a) a division that sells to wholly owned "branch distributors" and to nonCBS independent wholesaler distributors, both of which resell to subdistributors and retail record stores

[1] CX 264, pp. 34–35.

[2] These plants are located at (a) Bridgeport, Connecticut; (b) Pitman, New Jersey; (c) Terre Haute, Indiana; and (d) Los Angeles, California. The one located in Pitman, New Jersey, completed in May 1961, houses "the world's largest Lp [longplaying] manufacturing facilities," with "an annual capacity of 25 million Lp's." CX 264, p. 9; That is 14.4% of all LPs sold in the United States in 1961 (163 million). RX 441.

and (b) a wholly owned subsidiary corporation, Columbia Record Club, which retails the records directly to the consuming public, by-passing the wholesaler-retailer distribution channels. In 1961, and 1962, the Club's sales of records to consumers totaled $41.5 million and $53 million, respectively [3]: Columbia's non-club sales to the trade were approximately the same as its Club sales. In the aggregate, then, phonograph records accounted for somewhat less than 20% of CBS's total sales of $473.8 million in 1961.

3. This proceeding is concerned primarily with Columbia's formation and operation of its Columbia Record Club, an organization that distributes phonograph records direct to the consuming public through the "club" or "subscription" form of mail order selling. Under the "club" method of selling, the consumer becomes a "member" of the selling organization and "commits" himself to buy a minimum number of phonograph records over a stated period of time.

The principal features that distinguish the "club" from the nonclub (retail dealer or rack) method of selling and buying are as follows. The Club's initial communication with the consumer is accomplished by extensive advertising, principally in such national magazines as *Life, Look*, etc. These advertisements describe an "introductory offer" [4] under which the consumer, as an inducement to "join" the Club and

[3] CX 256, 783-e, and RX 422, *in camera*.

[4] For example: [T]he Club offers the biggest hits from Columbia—Mercury—Kapp—Liberty—United Artists—Warner Brothers—Epic and many other record companies! More Top Stars . . . More Savings . . . the greatest values ever offered by any record club! . . . fabulous savings . . . world's largest record club. By joining now, you can have your choice of ANY SIX of the 78 outstanding records shown on these two pages—up to a $36.88 retail value—ALL SIX for only $1.89. What's more, you'll also receive a handy record brush and

agree to buy a certain number of records at a fixed price over a stated period of time, is offered a number of records immediately at a nominal (below-cost) price.[5]

The basic "popular" LP carries a "list" price of $3.98 in both Club and nonclub channels. Discounting and the like among the retail dealers has reduced their average price, in recent years, by an estimated 25% below list, or to $2.98. The clubs, on the other hand, "discount" by "giving away" records designated as "free." Thus, at the time of these hearings in 1963, the Columbia Record Club's "introductory offer" to new members was six (6) records for an aggregate price of $1.89, plus 55c postage, or approximately 41c per record, provided the new member also agrees to buy *another* six (6) records in the next 12 months at the "list" price of $3.98 each, plus 35c postage on each, or a total of $4.33 per record. The total bill for the 12 records figures to $28.42, or $2.37 each.

In the second year, the Club member buys on a 3-for-the-price-of-2 basis. For each two he "buys" at the list price of $3.98, he gets a second one "free." Thus, he buys two for $3.98 each ($7.96), plus a 35c mailing and handling charge for each (70c), or a total of $8.66—for an average price of $2.88 per record.

After receiving the first six records under the "introductory offer," the new member buys his second six in accordance with what is called the "negative option plan." Every 28 days the Columbia Record Club mails to its members a 24-page magazine describing the 100 to 200 records currently being offered by

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cleaning cloth—an additional value of $1.19—absolutely FREE! . . . only membership obligation is to purchase six selections from the more than 400 to be offered in the coming 12 months. . . ." CX 731-B.

[5] Tr. 5144.

the Club, along with a card of the type used in data processing machines, called a "negative option card."[6] The card describes four (4) "options." First, the member can do nothing about the cards (*e.g.*, throw it away), in which case he will automatically be sent and billed for a phonograph record called that month's "current selection" of the Club "division" to which he belongs.[7] Second, the member can "check" a "box" on the card reading: "INSTEAD OF the current selection, send me the records I have checked on the reverse side." Third, he can check a box reading: "IN ADDITION TO the current selection, send me the records I have checked on the reverse side." Fourth, the member can check one saying: "CHECK here if you DO NOT wish to receive *any* records this month."[8] In practice, the Club's officials anticipate in advance that approximately 35% of the members of its largest ("popular") division will not return the card and hence will receive and accept the record selected for them by the Club.[9]

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[6] See RX 385, attachment to p. 19.

[7] The Club had four divisions until recently: Listening and Dancing; Classical; Broadway; and Jazz. A fifth division, Country and Western, was later added. Some 40% of the Club's total members are in the largest division, Listening and Dancing ("popular") division. The other three were of approximately equal size, about 20% each. The Club had approximately 2 million members in all divisions in November 1962. Tr. 5128.

[8] RX 385, attachment to p. 19 (boldface type in original; emphasis added). The member that wants no record at all in a particular month will of course still have to buy at least six (6) records over the commitment period of 12 months.

[9] Tr. 713–714. In one period, for example, the lowest "pull rate" of any record (percentage of members accepting the record selected for them) in the monophonic section of the Listening and Dancing Division was 25% (95,667 records sold); the highest had a pull rate of 34% (156,948 records

4. The Columbia Record Club itself was formed in August 1955. Thereafter, commencing in May 1958, Columbia decided the Club could be more profitably operated if it sold not just its own (Columbia) records, but those of some of its competitors as well. However, instead of going to those manufacturers' wholesale distributors (described here as the "open" market for phonograph records) and paying the same price paid by other record retailers (the Columbia Record Club is admittedly a "retailer," in that it sells directly to the ultimate consumer), the Club entered into a series of "licensing" agreements with nine (9) of its medium-size and smaller competitors under which it uses their "masters" to produce finished records at a total cost of some 87.5¢, versus the $1.60 or more all competing retailers (whether clubs or stores) are required to pay wholesalers for those same records. It also included in those "licensing" agreements provisions (a) fixing (depressing) the price (royalty) to be paid by those manufacturer-competitors to their own artists on records sold through the Columbia Record Club [10] and (b) giving

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sold). Tr. 8411. One of the Club's officials testified that the "current selections" sent automatically to members accounted for 48.4% of the Club's total *sales volume* in 1962. Tr. 8418, 8531–8532.

[10] Two of the earliest of these contracts also contained provisions (a) fixing the price at which the Columbia Record Club was to resell the competitors' records and (b) fixing the price at which those competitors were themselves to sell their records in nonclub channels, *i.e.*, to their own distributors (who in turn sell to retail stores). The evidence is not sufficient, however, to support a finding that these two price fixing agreements have continued in effect or that they were a part of the later licensing contracts.

The evidence on the fixing of artists' royalties, on the other hand, is clearly set out in several of the contracts, including the later ones. See Findings 10 and 11.

the Columbia Record Club the sole and "exclusive" right or "license" to fabricate records from those nine competitors' "master" records (for a royalty of some 17.8¢ on each record it fabricates from them), those competitors expressly promising (i) not to engage in a "club" operation themselves, (ii) not to sell their records directly to anyone else who resells them through a mail order "club" operation, and (iii) not to allow anyone else to use their "master" recordings for the purpose of producing finished records for resale through a mail order "club" operation.

5. Columbia established the Record Club for the purpose of preventing the entry of certain nonrecord firms, particularly *book* publishers and distributors. Columbia intended to thwart further competition not only in the sale of records but in the hiring of artists. In approximately the middle of 1951, Mr. Goddard Lieberson, then the executive vice-president of Columbia Records, initiated a series of meetings with an official of the Book-of-the-Month Club, Mr. Harry Scherman,[11] to see if there "was an area of possible working together with some one in the *book club* business to go into something of the record club type of operation."[12] Columbia concluded that the book club's approach was "not realistic" and dropped the matter. Then, in 1954, the book club initiated further meetings. Again, Columbia found the proposal unattractive. At the last of that series of meetings, however, in December 1954, the book club's official announced "that he had come to the *final decision that the Book of the Month Club under his management was definitely going into the record club business*, that he would repeat to us his interest in doing it in conjunction with Columbia Records, and when we told him

[11] Tr. 6168, *et seq.*

[12] Tr. 6170 [emphasis added].

that we did not have an interest in joining with him in this venture, he told us that, be that as it may, he should *warn us then that he would need important artists, and if they were ours, and some of them would be, he said, he would make an effort to get them under contract,* you know when their contracts with us had terminated."[13] This was later confirmed by several of Columbia's artists, who reported that they had in fact been approached by Book-of-the-Month Club with very attractive offers.[14]

Columbia's officials were concerned over this new competitive threat: "[*I*]*t was perfectly obvious that the club form of selling was the way of the future* and that Book-of-the-Month had already demonstrated through its Music Appreciation Record Club that it could make a successful club . . . Well, if the mail order people became powerful in the record club field, as they gave every indication of doing in 1955, it was entirely conceivable and in fact probable that *with the immense purchasing power that could be generated through mail order selling, the important recording artists would naturally gravitate to these companies.* . . . [Hence those artists] would be not available for retail, or at least would be available under such terms and conditions as might not be beneficial to the retail business."[15] "[I]t was soon obvious they [the book firms] would be able to go to artists and offer them better deals than we could."[16]

Columbia moved swiftly and effectively:

> Q. Before this was over, Mr. Adler, which Columbia artists did Book-of-the-Month Club actually sign?

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[13] Tr. 6173 [emphasis added].

[14] Tr. 6174.

[15] Tr. 5035–5038 [emphasis added].

[16] Tr. 4839.

A. I don't recall now whether they signed one or none. I think *we effectively thwarted it.*

Q. Is it possible that they didn't sign any Columbia artists?

A. I said I didn't know whether they signed one or none. *We effectively thwarted their plan.*[17]

This threat of new competition was particularly alarming because it came from outside the "industry" (records), posing the danger of entry by a complete stranger: "Well, we felt that several things could happen with a third party being in the business, a third party, I mean, other than the record manufacturer and the dealer and the normal distribution that goes to the dealer. We felt that if the important artists were siphoned away into a club there was a reasonable possibility that they would never find their way to the retail business; therefore, the retailer would suffer. We would also suffer by not having these artists." [18]

6. Columbia's purpose in entering into the licensing contracts with its competitors included, in addition to the obvious one of increasing the club's sales and market share, the desire to prevent those competitors from entering the club field on their own or from selling their records to anyone else who attempted to sell in that club field. The first contract between Columbia and its competitor-licensors, the one with Caedmon dated May 15, 1958, granted Columbia "the *exclusive* right, privilege and license" to "use the master recordings" of Caedmon in the manufacture and sale "through our mail order record club," Caedmon agreeing that it would "not sell *by mail order methods* of any kind or nature whatsoever, and [would] not authorize or consent to such sale *by any*

[17] Tr. 5043–5044 [emphasis added].

[18] Tr. 6177–6178.

third party, of phonograph records manufactured from any of the master recordings, or from copies or duplicates thereof."[19] This provision was amended 11 days later, May 26, 1958, to make it somewhat more specific as to the channel of distribution aimed at and the competitors Caedmon was not to sell to: "You [Caedmon] agree that, during the term of this agreement, you will not distribute or sell or authorize or consent to the distribution or sale by any third party of phonograph records manufactured from any of the master recordings, *through any mail order record club* which regularly distributes or offers for sale to its members significant quantities of phonograph records of a musical nature, *including*, without limitation, the '*Book-of-the Month Club*,' '*Music Treasures of the World*,' any *RCA Victor* record club, and any *Capitol* record club."[20]

In other words, the restriction on Caedmon was reduced from the broader channel ("mail order methods of any kind or nature whatsoever") to the narrower one ("any mail order record *club*"), and four competitors of the Columbia Club were specifically named as examples of the competing "clubs" Caedmon was forbidden to sell to. (Caedmon remained free, however, to sell its records through normal retail channels.)[21]

7. The second of these contracts, the one with Verve dated March 31, 1959, similarly granted Columbia the exclusive "right, privilege and license" to manufacture and sell phonograph records made from certain specific Verve "Licensed Masters" through the club

[19] CX 19, pars. 3(a) and 4(c) [emphasis added].

[20] CX 20 [emphasis added].

[21] "It is understood and agreed, however, that nothing herein contained is intended to or shall in any way restrict the distribution and sale of such phonograph records through normal retail channels." CX 19, 4(c).

channel, *i.e.*, "by direct mail in accordance with the merchandising method known and understood, in the mail order business, as the 'subscription' or 'club' plan as distinguished from individual over-the-counter sales by retail store outlets receiving their phonograph records from phonograph record distributors. . . ." [22] "You [Verve] agree that during the Term of this agreement you will not, in the territory of the United States and Canada, (1) sell by direct mail, (2) offer for sale by direct mail, or (3) authorize or consent to the sale or offering for sale by direct mail by any third party of phonograph records manufactured from master recordings which you now own or control or which you may hereafter own or control." [23]

8. The third of these agreements, the one with Mercury dated April 1, 1960, granted the Columbia Club "the sole and exclusive right, privilege and license" to manufacture and sell records made from Mercury "master recordings" by "direct mail in accordance with the merchandising method known and understood, in the mail order business, as the 'subscription' or 'club' plan as distinguished from individual over-the-counter sales by retail store outlets receiving their phonograph records from phonograph record distributors. . . ." [24] It further provided: "You [Mercury] agree that during the term of this agreement you will not, in the territory of the United

[22] CX 23, p. 3.

[23] *Id.*, pp. 7–8. Certain records are excepted from this provision, under certain described circumstances. Thus, it was agreed that "you [Verve] will not authorize any other mail order record club (hereinafter referred to as 'other club'), such as the Capitol or RCA Victor Club, to release phonograph record albums embodying the performances of Ella Fitzgerald or Oscar Peterson except" in certain described circumstances. *Id.*, p. 4.

[24] CX 34, p. 2, par. 2.

States and Canada, (1) sell by direct mail, (2) offer for sale by direct mail, or (3) authorize or consent to the sale or offering for sale by direct mail by any third party of phonograph records manufactured from master recordings which you now own or control or which you may hereafter own or control."[25]

9. The remainder of the contracts contain similar provisions giving the Columbia Club the "sole and exclusive" right to use the licensor's masters to produce records for sale by the "club" method and expressly prohibiting the licensor from selling in competition with the Columbia Club or allowing anyone else to use its masters to do so.[26]

10. Certain of these contracts between Columbia and its competitors also contain express provisions fixing the prices (royalties) to be paid by these companies to artists who record for them. Thus the contract with Verve (March 31, 1959) provided that

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[25] *Id.*, p. 3, par. 7.

[26] Respondent attaches significance to the fact that the contracts do not run in perpetuity, but are limited in time—*e.g.*, Cameo-Parkway, 1 year; Caedmon, 2 years and 1 month; Kapp, Liberty, and United Artists, 3 years and 4 months; and Mercury, 3 years and 6 months. However, several of them contain express "options to renew" and they are in practice regularly renewed.

Columbia also emphasizes the fact that the more recent of the contracts contain "release" clauses giving the licensor-competitors an option to either take individual records ("partial" release) or entire catalogs ("complete" release) out of the Columbia Record Club and put them in another club if they get a better offer from such other record club. (The Caedmon, United Artists and Liberty contracts contained both types of release clauses, and the Kapp contract had a "partial" release clause only.) There has been no significant use of these clauses, however, and the licensors make it clear that they like their arrangements with the Columbia Record Club and have no intention of allowing their records to be offered through any other club. See, *e.g.*, tr. 1594–1595.

Verve would attempt to get its artists to agree to accept (a) a 50% reduction in their royalty rate on their records *sold* through the Columbia Club, and (b) a complete waiver of any royalty payment at all on those of their records that the Club should give away *free* to its subscribers as "introductory offer" or "bonus" records.[27] The contract recognized, however, that Verve might be "unable . . . to obtain execution [by the artist] of a modification agreement substantially in the form attached hereto as Exhibit I," and provided that, in such event, Verve was to notify Columbia of this recalcitrant artist within 15 days. "We shall then have the right to negotiate directly with any such artist to obtain the execution of any such modification, but in the event we shall be unsuccessful, we agree that such master recording shall not be deemed to be included in Schedule A or C of this agreement [records to be used by the Club]. With reference to such direct negotiation, if we obtain a modification whereby the artist is to be paid a royalty in excess of fifty per cent (50%) of the royalty payable to you hereunder, with reference to such Licensed Master, the royalty payable to you pursuant to paragraph 12 [five (5) per cent of the royalty price with respect to ninety per cent (90%) of our net sales] shall be increased to a figure no less than two and one-half percent (2½%) greater than that payable to

[27] CX 27–a, 28–a. While Verve was to use its "best efforts" to obtain this kind of concession from its artists, Columbia said that "we agree to accept" in lieu of the one described, a modification "similar to Exhibit II. . . ." CX 29-b. That "Exhibit II." prepared for the signature of the artist, provides in part: "I agree to waive [all] my royalties . . . on all records sold via mail order under the 'subscription' or 'club' plan. . . . I have received $500 as payment in full for this waiver." CX 30.

the artist." [28] Thus, taking $3.46 as the "royalty price" on a $3.98 list price record, Verve was to get 17.3¢ (5% of the royalty price) on 9 out of every 10 of its records sold by the Club. But if the artist insists upon more than half of that 17.3¢, it would be raised to the point where Verve could pay the artist his full price and still realize 8.6¢ (2½% of the "royalty price," $3.46).

11. Another of Columbia's contracts with its competitors, the one with Mercury (April 1, 1960), was still more explicit on the subject of suppressing competition in bidding for artists' services: "You [Mercury] recognize that it is our [Columbia] policy to pay no more than half of customary artist royalty with respect to recordings sold by us by our direct mail operation, and agree in general to conform to this policy, except, in cases of artists who are dead or no longer under contract to you." [29] This provision con-

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[28] CX 23, pp. 19–20, par. 25. This provision continued: "Nothing contained in this paragraph shall alter the concept that all royalty payments to artists are to be made directly by you; and in that regard, we [Columbia] will send a copy of any modification obtained by us to you within five (5) days after such modification has been executed by the artist." *Ibid.*

The royalty provisions in at least one of the other contracts expressly designated the artist's share: "We [Columbia] will pay you [Vanguard] a royalty of five (5) per cent of the royalty price plus an additional artist royalty of two and one-half (2½) per cent of the royalty price. Said royalty shall be paid on ninety (90) per cent of our net sales of Albums manufactured from the master recordings. Net sales are defined as gross shipment less returns." CX 43, p. 3, par. 7.

[29] CX 34, p. '6, par. 13. It was further provided: "You [Merdury] will make your best efforts to make available to us under the terms of this agreement the performances of major artists who are now under contract to you or who have previously been under contract to you, and will supply us by May 31, 1960, with a list of those who are not so available. If this list in our view is so material to the terms of this

cluded: "Nothing herein shall prevent you [Mercury] from absorbing or paying on your own behalf any additional royalty on records sold by us to any of your artists. You will, however, advise us on request of any such additional payments or agreements to pay, and you agree that we shall not be liable for any royalty beyond that specified in paragraph 11 [7½% and 10%, respectively, on nonclassical and classical records, figured on 95% of net sales]." [30]

Similar provisions were contained in Columbia's contracts with its other competitors.[31]

12. While there are no provisions in the written contracts between Columbia and its competitors that deal with the matter of not attempting to hire away each other's artists, the record is clear that there is, in fact, an understanding or agreement among them to lessen their competition in this respect. Thus, one of Columbia's licensor-competitors was asked about an

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contract that we deem it impossible to meet the guarantee herein provided, we shall so notify you within ten days thereafter and shall then be obliged to pay only such royalties pursuant to paragraph 11 as are earned on items already used or announced by us and not on the royalty guarantee as provided in section 11 hereof. Except for payment as such this contract shall thereupon be terminated.

"You agree that the performances of any artists signed by you subsequent to the date of this contract and to be performed before the termination thereof shall be available to us pursuant to the terms of this agreement." *Ibid.*

[30] *Ibid.* As a Columbia official explained the situation in a letter to Mercury: "It has been my experience—and of course I will be glad to defer to your judgment in this matter—that once you *truckle* to an artist, it is very difficult to get the artist in line again." CX 358(c)-(d) (emphasis added).

[31] Warner Brothers, CX 39, p. 5, par. 11; Kapp, CX 41, p. 7, par. 13; Vanguard, CX 43, p. 4, par. 9; United Artists, CX 44, p. 6, par. 13; Liberty, CX 45, p. 6, par 13; Cameo-Parkway, CX 453, p. 6, par. 13.

incident in which Columbia had let him know that one of his artists had offered his services to Columbia:

> Q. Is this one of the advantages of being in the club, by the way?
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> A. I wouldn't say it is one of the advantages of being in the club. I can think of many other significant advantages. I would say that is possibly, one could consider this a *fringe benefit*.[32]

13. Several alternative "markets" have been suggested as the appropriate area in which to evaluate the probable competitive effects of these licensing agreements, including (1) the "all-record," (2) "all-LP," (3) "all-mail-order," and (4) the mail order "club" markets. The one advanced by respondent is the "all-record" market, *i.e.*, all phonograph record sales in the United States, including both "LP"[33] and "singles," and including sales made through all channels of distribution—retail stores, "racks,"[34] juke

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[32] Tr. 3676 [emphasis added].

[33] "LP" is an abbreviation of "long-playing," a record that generally contains six (6) songs or performances on each side (usually 3 minutes of playing time per song), for a total of 12 songs or performances per record (36 minutes), as contrasted with the "single," which has only one (1) song or performance on each side (6 minutes playing time on both sides). The two records also differ in diameter and in turntable speed: the LP is 12 inches in diameter and revolves at a speed of 33⅓ revolutions per minute, while the "single" is 7 inches in diameter and turns at 45 revolutions per minute. The two also sell at different prices—the LP "list price" is $3.98 and up, the "single" 98¢–99¢. The LP accounted for about 75% of total phonograph record sales in 1961.

[34] "Racks" are the familiar structures displaying phonograph records in supermarkets, drug stores, and other high-traffic retail areas. Their distinguishing characteristic is that, unlike the retail record dealer's store, which may carry virtually all of approximately 25,000 separate records offered for sale by all record manufacturers, frequently carry only the 50–150 most popular records (the current "hits").

boxes, and "clubs."[35] In 1960, total consumer expenditures for all kinds of records, through all channels, were an estimated $521 million.[36] Columbia's share of this total was an estimated 21.2%.[37] The other two members of the phonograph record industry's "big three," RCA and Capitol, had an estimated 16% and 11.1%, respectively, of the all-record market. Decca, Mercury, and MGM followed with 3.4%, 2.7%, and 2.4%, respectively. Some 20 other firms shared the bulk of the remaining 43.2%.

Firm:	*Share of 1960 All-Record Sales (percent)*
Columbia	21.2
RCA	16.0
Capitol	11.1
"Big Three" Total	48.3
Decca	3.4
Mercury	2.7
MGM	2.4
All others	43.2
	100.0

[35] The relative share of each of these four (4) channels of distribution in the consumer's total expenditures on phonograph records in 1961 was estimated as follows (CX 199a):

Channel of Distribution	1961 Sales	
	Dollars (Millions)	Percentage
Retail Stores	$305	52
Racks	147	25
Clubs	100	17
Juke Boxes	35	6
Totals	$587	100

As noted below, the "club" figure for 1961—$100 million—was later scaled downward, that figure being estimated as closer to actual Club sales in the following year, 1962, when the "universe" had grown to an estimated $620 million. This would give the clubs' 16.1% of all record sales in the latter year.

[36] CX 199b.

[37] RX 350.

CBS produces a somewhat larger share of all "LP" (long-playing) records,[38] that is, exclusive of "singles"[39]:

Firm:	*1960 Share of "LP" Sales*
Columbia	25.4%
RCA	17.5
Capitol	13.6
"Big Three" Total	56.5
Decca	3.3
Mercury	2.1
MGM	1.8
All others	36.3
	100.0%

In what is referred to in this record as the "mail order" channel of distribution—the sale of phonograph records through the mail by all types of organizations, including sales by mail order houses, "clubs," etc.—respondent offers the following share data:[40]

Firm	Share of All Phonograph Record Sales by "Mail Order"	
	3d & 4th Qtrs., 1961	1st 3 Qtrs., 1962
Columbia	47.1%	44.0%
RCA	18.3	20.8
Reader's Digest	17.6	18.2
Capitol	9.6	8.1
All others	7.4	8.9

In the still narrower "club" channel of distribution—that is, the sale of phonograph records through the "membership" or "subscription" method of mail

[38] As noted, LP's account for approximately 75% of all phonograph record sales.

[39] RX 354.

[40] RX 450.

order selling as described below—CBS accounts for more than 50% of total sales: [41]

14. The significance of the specific sales volume acquired by Columbia under the challenged "licensing" agreements (some $12.8 million in 1961) is similarly affected by the choice of the "relevant market." First, if there is only a single "all-record" market for phonograph records in the United States, then the *total* sales of the Columbia Record Club—including both its

[41] CX 357. Some market share data is available for two later years, 1961 and 1962, but it is not as complete for all channels of distribution as the 1960 figures set out above. One index for the all-record market is available, an index based on a comparison of individual record manufacturers' payments of excise taxes with *total* excise tax collections. This shows Columbia with 16.52% in 1960, 18.47% in 1961, and 20.72% of the all-record market in 1962. RX 418, *in camera*. Columbia contends that its share of all "club" sales fell from 56.1% in 1960 (as shown above) to 41.5% in 1961. RX 451, *in camera*. No such decline occurred. In fact, sales of the Columbia Record Club increased from $30.4 million in 1959, to $37.5 million in 1960, to $41.5 million in 1961, and to $53.2 million in 1962. CX 783-e and RX 422, *in camera*. Certainly no greater increases occurred in the sales of the club sector as a whole. The alleged decline in its share in 1961 is based on the fact that the "universe" figure—sales of all clubs—is not an exactly known figure but one estimated by *Billboard*, the industry's statistician, which admittedly "overestimated" the 1961 universe figure (putting all club sales at $100 million) and thereby giving Columbia a fictitiously lower "share" of that inflated total. *Billboard* later put the 1962 figure at $100 million, scaling the 1961 figure downward accordingly.

Firm:	*1960 Share of All Phonograph Record Sales Through "Clubs"*
Columbia	56.1%
RCA	26.8
Capitol	7.7
"Big Three" Total	90.6
All others	9.4

own Columbia records *and* those licensed from its competitors—do not constitute a dominant market share. Measured against the 1961 "universe" figure of $587 million, the Columbia Record Club's sales of $41.5 million in 1961 constituted some 7.07% of all phonograph records sold to consumers in that year. Of that $41.5 million total, $12.8 million of it (30.9%) represented the Club's sales of the nine (9) competitors' records under the challenged licensing agreements. Measured against the over-all, all-record universe figure of $587 million, that $12.8 million sales volume acquired by Columbia from its competitors amounts, therefore, to only 2.19% of all phonograph record sales through all channels of distribution. Stated another way, acceptance of an "all-record" market as the relevant market would mean the situation is one in which Columbia, with slightly less than 20% of that over-all market, on its own labels, has "acquired" by contract another 2.19% from its competitors.

A much more concentrated structure is presented, however, if the sale of phonograph records through the "club" channel of distribution is itself considered a separate market, set apart from the over-all record market by meaningful economic factors. The Columbia Record Club had, as noted, 56.1% of the sales of all record "clubs" in 1960 and at least 53% in 1962. The latter figure is, we believe, a conservative estimate of its share in the intervening year, 1961. As noted above, its 1961 sales, in dollars, were $41.5 million, with $12.8 million (30.9%) being accounted for by its sales of competitors' records. This means that, *without* the sales volume acquired pursuant to these challenged licensing agreements, the Columbia Record Club's 1961 sales would have been $28.7 million, or $12.8 million less. In terms of percentages, it would have had

not 53% of all sales through the "club" channel of distribution but some 37%, about 16 percentage points less. Stated another way, the existence of an economically meaningful "club" market would mean the situation is roughly one in which (1) a firm with some 37% of the relevant market already ($28.7 million) has acquired another 16 percentage points by contract with nine of its competitors ($12.8 million), for a total of approximately 53%, and (2) in which that firm and two others have more than 90% of the relevant market.[42]

15. There is no persuasive evidence here that the sale of phonograph records through clubs and through nonclub mail order methods combine to make up an economically meaningful "mail order" market. The principal category of sales proposed for this "market," other than Club sales, is the sale of what are called record "packages," *i.e.*, groups of records sold as a unit in a single mail order transaction. *Reader's Digest* magazine is the largest seller[43] of such pack-

[42] Using the Columbia Record Club's actual sales figure for 1962, $58 million, and assuming that the licensors' contribution to that total remained at no more than the 30.9% they accounted for in the prior year, 1961, then the two components of the Club's 1962 sales of $53 million would have consisted of (1) $36.6 million on Columbia's own labels, plus (2) $16.4 million on the licensors' labels. (In units, the nine licensors' records constituted 36.3% of all records shipped by the Columbia Record Club in 1962—8.1 million out of the total of 22.3 million LP's it shipped. CX 823, *in camera*.) Dividing each of these figures by the 1962 "club" universe of $100 million gives 36.6% as the approximate share of the club market of Columbia's own labels, 16.4% as that of the nine licensors, for a combined total of 53%.

[43] The principal sellers of "packages" are *Reader's Digest* magazine, *Life* magazine, Book-of-the-Month Club, Columbia, and Sears Roebuck. Tr. 10,157. *Reader's Digest* gave its phonograph record sales in terms of an "average" figure for the years 1960, 1961, and 1962 as $12.1 million. RX 700, *in camera*. (Its sales

ages, with sales of some $12.1 million in 1962,[44] a figure that would be equivalent to approximately 12.1% of all "club" sales in 1962 ($100 million) or approximately 2% of all record sales, through all channels of distribution ($620 million in 1962).

The "package" records sold by *Reader's Digest*, however, are *not the same records* that are sold in the "clubs." Some of the records sold in these packages bear the same titles, and were performed from the same published music scores, but the *artists* are not the same. The official in charge of Reader's Digest's package operation testified that these package records consist primarily of "war horses" or "standard repertoire" (*e.g.*, Beethoven's symphonies) performed by orchestras and performers that are generally unknown to the American public; no "name" artists are

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in 1957 had been $7.8 million. *Ibid.*) Both *Life* magazine and Book-of-the-Month Club had total phonograph record sales of $1 million or less in 1962. RX 502 and 507–508, *in camera*. This latter figure is some 1/8th of 1% of the industry's approximately $620 million total sales and less than 1% of the estimated $100 million of all "club" sales in that year (RX 311, *in camera;* tr. 6867, 6931).

[44] *Ibid.* These "package" sales of *Reader's Digest* are separate and distinct from its sales through a "club" operation it conducts as a selling agent for RCA. In the package business, *Reader's Digest* sells records manufactured by RCA but bearing its own "Reader's Digest" label. In the other operation, it is under formal contract to "act as [RCA's] agent in developing, advertising, promoting, and servicing [RCA's] Record Clubs." RX 704–a (contract between RCA and *Reader's Digest*); tr. 9459. The RCA Club (administered by *Reader's Digest* has a much larger sales volume, approximately $14 million in 1961 and $22.7 million in 1962. RX 645. The latter figure would be approximately 22.7% of the estimated $100 million total "club" sales in 1962 (compared to the Columbia Record Club's $53 million, or 53%).

used as performers, and hence the records "cost less" [45] and sell for less. This is precisely the opposite of the situation in "club" selling. As discussed below, the records sold in clubs feature the artist and his personality, rather than the repertoire itself, and hence sell largely those records that carry the performances of well-known, highly publicized artists. In the one case, the seller is attempting to sell the repertoire alone (*e.g.*, Beethoven's Fifth Symphony); in the other, he is selling the artist (*e.g.*, Columbia's Leonard Bernstein).[46] Supply and demand conditions are obviously not the same in the sale of these two entirely different records. One of respondent's own officials implicitly recognized this. "They [Book-of-the-Month Club] are now *out* of the record club business. They are *in* the business of selling records by *mail order*." [47] The *Reader's Digest* official in charge of its "package" operation testified that "I don't think the package business is in competition with the record club business." [48] With different performers, different costs, and different prices, the "package" record and the "club" record are clearly in different markets.

16. In view of our findings below that club sales are in a market by themselves and constitute the relevant market involved in this proceeding, it necessarily follows that "singles" are not a part of that market; only "LP's" can be economically marketed through the club channel of distribution.[49]

17. We find that the "relevant market" involved here is the sale of phonograph records through what respondent describes in its own licensing contracts as sale "by direct mail in accordance with the mer-

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[45] Tr. 10,114–10,115; 10,146–10,150.

[46] See, *e.g.*, tr. 10,159–10,164; 10,623–10,635; 10,661–10,673.

[47] Tr. 5073 [emphasis added].

[48] Tr. 10,123.

[49] Tr. 4894.

chandising method known and understood, in the mail order business, as the 'subscription' or 'club' plan as distinguished from individual over-the-counter sales by retail store outlets,"[50] *i.e.*, the relevant market is the sale of records through the "club" channel of distribution.

First, as discussed in some detail above,[51] this record is replete with evidence of respondent's *intent* to exclude competing clubs from that marketing channel. And a purpose to exclude others from an area necessarily implies a conviction that it constitutes an economically meaningful market, because otherwise there would be no potential economic gain from the exclusion. Respondent's own belief that the exclusion was from an economically meaningful market is inherent in the language of the contracts:

> You [Caedmon] agree that, during the term of this agreement, you will not distribute or sell or authorize or consent to the distribution or sale by any third party of phonograph records manufactured from any of the master recordings, *through any mail order record club* which regularly distributes or offers for sale to its members significant quantities of phonograph records of a musical nature, including, without limitation, the "Book-of-the-Month Club," "Music Treasures of the World," any RCA Victor record club, and any Capitol record club.[52]
>
> * * *
>
> You [Mercury] agree that during the term of this agreement you will not, in the territory of the United States and Canada, (1) sell by direct mail, (2) offer for sale by direct mail, or

[50] See, *e.g.*, CX 23, p. 3.

[51] Finding 5.

[52] CX. 20.

(3) authorize or consent to the sale of phonograph records manufactured from master recordings which you now own or control or which you may hereafter own or control.[53]

18. A finding that the relevant market here is the sale of records generally would require a finding that phonograph records sold through local retail stores, "racks," and juke boxes are adequate "substitutes," as far as the consumer is concerned, for records sold through "clubs," *i.e.*, that, as to a given record[54] being offered at the same price, the consumer is indifferent as to which channel of distribution he patronizes. This is clearly not the case. First of all, the prices are not the same. There is an entirely different price structure on records sold through clubs and those sold through nonclub channels. In the nonclub sector, the "suggested retail prices" (prices the manufacturers suggest their dealers charge consumers)

[53] CX 34, p. 3, par. 7. See also Findings 6, 7, 8 and 9.

[54] The records sold through the Columbia Record Club are admittedly physically identical to records sold through dealer stores, racks, and juke boxes, *e.g.*, Andy Williams' "Moon River" (recorded by Kapp Records, one of the nine competing manufacturers that signed a "licensing" agreement with the Columbia Record Club) is simultaneously sold through the Columbia Record Club and through these other retail outlets. In other words, there is no "product differentiation" involved in the definition of the relevant market here. As noted below, however, this does not mean that club and nonclub outlets have exactly the *same repertoire* in all respects: the Columbia Record Club limits itself primarily to "hit" records, offering some 100–200 records per month (about 1,500 per year) to its Club members, whereas retail dealers often carry the entire 25,000 separate records currently offered by all of the country's record manufacturers. The point is simply that, on each of the small number of "hits" that the Club *does* elect to handle, physically identical copies of that precise record—the same song, same performer, etc.—are in fact being offered for sale to the consuming public at the same time by other retail outlets.

are as follows: (a) "popular" records, $3.98; (b) "classical" records, $4.98; (c) "broadway show tunes," $5.98.[55] While respondents have adequately demonstrated that dealers in some of the smaller towns do in fact charge these full list prices, there was evidence that the "average" dealer price has been reduced ("discounting," etc.) by some 25%, to approximately $2.98 on a "popular" ($3.98) record. The "club" price to the consumer, on the other hand, is approximately $2.37 for exactly the same record, a difference of more than 20% between the club and nonclub prices to the consumer. If consumers were in fact indifferent as to which channel of distribution they bought their records through, making their choice solely on the basis of price, then the club channel would necessarily have all of the business on those particular records it elected to sell, and the nonclub sector would have none.[56] It is clear, then, that consumers do in fact distinguish between the various channels of distribution.

19. The so-called "disadvantages" of buying through club versus nonclub outlets—limited selection to choose from, having to wait from a month to six (6) weeks before the records arrive, not being able to play them before buying, and the necessity of making a "commitment" to buy six (6) records

[55] These are the prices for monaural records; stereo records are $1.00 more. "Singles," which constitute some 25% of all record sales, have a suggested list price of 98¢–99¢.

[56] One of the Columbia Record Club officials testified that the larger part of the record-buying public obviously thinks there are some "disadvantages" in buying through the "club" channel because "otherwise, we would have *all* of the sales of records through clubs rather than at retail. . . ." Tr. 4929 (emphasis added). As noted, the clubs accounted for something less than 20% of all record sales in 1962 (less than $100 million out of a total of an estimated $620 million).

at $3.98 each (plus mailing costs) over a period of a year—are obviously evaluated differently by different people. The clubs have their primary appeal to persons having certain characteristics, most particularly those having (1) a propensity to shop by mail,[57] (2) a desire to develop a phonograph record "collection,"[58] (3) a desire for "guidance" or expert assistance in developing that record collection[59] and (4) an active interest in buying at economical prices.[60]

More specifically, the individuals that join phonograph record clubs tend to be (1) young adults, who have (2) just purchased a phonograph record *player,*[61] who are (3) relatively uncertain in their own musical preferences, and who, having purchased other (non-record) items by mail in the past, (4) have no particular reluctance to buy records in that manner. These characteristics make up a record buyer that is, in the phraseology of Columbia's market researchers, "susceptible to club values,"[62] *i.e.,* a buyer that believes the clubs' "advantages" (20% lower price, the convenience of arm-chair buying,[63] expert "guidance" in developing a well-rounded collection of "hits," etc.) far outweigh its "disadvantages."

20. Columbia's officials recognize the distinctive characteristics of the people who make up the "club" market for phonograph records, particularly the fact that they are "new collectors" who are only temporarily "susceptible" to club values and who will soon "outgrow" the Club or cease to be one of its potential customers. For the Columbia Record Club as a whole,

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[57] RX 320. Tr. 8338–8342.

[58] RX 340. Tr. 7959, 8315, 8320–8321.

[59] Tr. 8305.

[60] Tr. 8315, 8323.

[61] RX 337. Tr. 7944–7945, 8308–8309.

[62] See RX 340.

[63] Tr. 8319, 8323.

the long-run "shrinkage rate," *i.e.*, percentage of members resigning during the year, is 54.13%. This means that, of any hypothetical group of 100 new members enrolled at the beginning of any particular year, 54 of them would have dropped out by the end of the year.[64] The "club market," in short, is composed of those members of the record-buying public whose characteristics, at a particular period of time, make them regard the club's features as "advantages," not disadvantages, and who are thus responsive to the club's substantial price advantage over nonclub channels.

21. To the new collector who considers the "club" method of buying generally equal to or at least not decisively inferior to shopping for records in retail stores, price tends to become a highly significant factor. That is to say, in the area of "overlap" in product between the "clubs" and nonclub retail outlets,[65] a consumer "susceptible" to club values can be induced by the clubs' approximately 20% lower price to purchase his entire requirements *of those particular records* from them, buying none of those specific records in the retail dealer market. A club member who has just committed himself to buy 12 records from a club for $2.37 each (including postage) may well buy *other* records at his local retail dealer's store for $2.98, but not one of the 12 "hits" selected from the club's offerings at the lower price (and, to him, greater convenience). In the sale of those 12 records, to this particular consumer (and, therefore to the other three to four million club members like him), the clubs of the

[64] RX 365. Tr. 8406.

[65] The three clubs offer, as noted, 200–400 records to their members in any given month, or less than 2% of the 25,000 records offered for sale in the retail stores. It is only in the sale of those relatively few records that there is any "overlap" between the offerings of the two channels of distribution.

"big three" have no economically meaningful competition. This particular portion of the record-buying public—the young adults just beginning their record collections, those who have a relatively high propensity to shop by mail, etc.—is highly "susceptible" to the clubs' offer of this distinctive group of records ("hits") at a sharply differentiated price (20% lower), and hence constitutes a separate "market" in which different conditions of supply and demand operate than those present in the other channels of distribution.

22. The Columbia Record Club is able to profitably sell records at a lower price than those same records can be sold through nonclub retail outlets because it enjoys a substantial cost advantage over those other channels of distribution. That is to say, the "club" market is characterized not only by different "demand" conditions, but by different circumstances on the "supply" (cost) side as well. The cost structure in the club retailing of phonograph records is entirely different from the cost structure in nonclub record retailing. The Columbia Record Club presented data showing total costs per licensor record shipped by the Club in 1962 as $2.13, broken down as follows: [66]

Acquisition cost (mfg., royalties to licensors, etc.)	87.5¢
Free merchandise	12.3¢
Advertising costs	35.3¢
Sales promotion costs	17.2¢
Other operating and distribution costs	28.9¢
Bad debts	31.8¢
Total	$2.13

[66] Tr. 10,469–10,470, 10,937. The 87.5¢ "acquisition" cost is itself broken down as follows (CX 821, *in camera*):

Manufacturing cost	42.8¢
Royalties to licensors	17.8¢
Copyright royalties	13.7¢
AFM Fees	2.4¢
Excise tax	10.8¢
Total	87.5¢

23. In the nonclub sector (*e.g.*, the manufacturer-wholesaler-dealer chain), the outlet at the end of the chain that is said to compete with the clubs, the dealer, necessarily incurs total costs that substantially exceed those of the club, no matter how efficient he might be. Instead of the 87.5¢ the Columbia Record Club pays for the records of Liberty, Kapp, Warner Brothers, and the other licensors, the dealer structure (there are some 5,000 or more phonograph record dealers in the country) pays a price that ranges from a low of about $1.60 to a high of $2.47.[67] Columbia's own

[67] The "list" price structure of the industry calls for (on the "popular" record) a manufacturer-to-wholesaler price of $1.89 to $1.92; a wholesaler-to-dealer price of $2.47; and, finally, a dealer-to-consumer price of $3.98. There is, however, considerable "discounting" at two of these levels and, by some of the smaller firms at least, at all three of them. Thus, one distributor testified that, while "to many customers [retail dealers] we got as high as $2.47" per record, "[t]o the customer which had the most preference by size and things of that sort, the lowest we would get down is between $1.80 and $1.85." Tr. 1427. Many dealers, however, apparently pay the full "list" price of $2.47 for the majority of their records. See, e.g., tr. 832–833; 1267–1273; 2219–2221; 2893–2897; 3261; 3301–3302; 3392–3393; 5705–5706. Even Goody's, a large dealer in New York City, testified that "$2.47 is the norm" and that $2.00 "[is] the best deal" it can get. Tr. 1284–1285.

The wholesaler cannot sell for much less than that $1.80 figure since he pays his own manufacturer-supplier a minimum of at least $1.60. Thus, one wholesaler testified that "the best deal that I as a distributor can get . . . can bring my price [from the manufacturer] down to about $1.61 . . . ." Tr. 1418. Operating expenses would add "at least five or more percent to that figure," tr. 1419, bringing the total to $1.69. This range is corroborated by the testimony of one of the smaller manufacturers, Audio-Fidelity (developer of the stereo record), that it sometimes sells to wholesalers "for $1.60 or $1.70." Tr. 2025–2026. (Columbia, however, apparently gets the full "list" price from its wholesalers. In 1961, its LP sales to its wholesalers on its own "Columbia" label totaled $30,332,000 in dollar volume

dealers paid in 1961, after all "discounts" had been taken into account, an "average" price of $2.12 per record. While the price paid for records is presumably the largest single item of cost to the dealers, it is not the only one. The addition of all operating and overhead costs would undoubtedly bring the costs of even the largest and most efficient phonograph record dealer substantially above the $2.13 costs incurred by the Columbia Record Club in its operation. To the extent that the nonclub sector has higher costs than the clubs, its capacity to compete with them is proportionately reduced and the products it offers, at the higher prices its greater costs force it to charge, become progressively less acceptable as "substitutes" to the consumer. Here the thin profit-margins of the many dealers that testified in this proceeding,[68] on the one hand, and the evident satisfaction of the Columbia Record Club with its profit-margin,[69] on the other, raises a fair inference that the difference in the prices charged ($2.37 by the clubs versus an average of $2.98 by the dealers) is more than accounted for by the difference in their cost structures. Different prices and different costs are two of the principal hallmarks of economially separate markets.

24. The source of the Columbia Record Club's advantage over the nonclub sector, the ability to acquire records for 87.5¢ that cost nonclub retailers $1.60 or more, is also one of the primary factors responsible for the highly concentrated structure of the "club" submarket. On its own (Columbia label) records, this cost advantage stems simply from the fact of integra-

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and 16,600,000 in units sold, for an average price of $1.93 on each "Columbia" LP sold to its wholesalers that year. CX 253, *in camera*.)

[68] See, *e.g.*, tr. 2149; 2185–2186; 2273–2274; 2345; 2397–2400; 2467–2471; 2554–2555; 2660; 2692; 2797–2798; 2811; 2957.

[69] Tr. 8532.

tion, *i.e.*, from the fact that Columbia, in its role as a manufacturer, can "sell" records to its retailing arm (the Columbia Record Club) at a lower price than it charges outside distributors (wholesalers and retailers). RCA and Capitol, being similarly integrated from manufacturing to club retailing, presumably enjoy a similar position. The principal issue in this proceeding, however, is not integration, as such,[70] but the use of the restrictive "licensing" agreements described below to foreclose potential competitors from, and hence artificially maintain a noncompetitive structure in, the "club" market. In substance, those agreements enable the Columbia Record Club to enjoy the same cost advantage over potential entrants into the *club* market that it enjoys over retail dealers in the nonclub market. As noted, they enable the Club to acquire the records of these nine (9) medium-sized and smaller competitors at a total cost of 87.5¢ per record,[71] while expressly prohibiting those competitors from selling directly to any other club, on any terms whatsoever, a restriction that would compel another club desiring to handle the records of those nine producers to go to the latters' wholesalers and buy them at the "open market" price (wholesaler-to-dealer) of at least $1.60. This imposes on potential entrants into the club market an immediate cost disadvantage, vis-a-vis the Columbia Record Club, of at least 72.5¢ ($1.60−87.5¢=72.5¢). The magnitude of that disadvantage is illustrated by the fact that, ac-

[70] While the complaint in this matter charged a form of "dual distribution" (selling direct to consumers, in competition with Columbia dealers, at a price ($2.37) that is lower than the price charged by the Columbia factory to Columbia dealers ($2.47) for the same Columbia records), the evidence of injury to competition at the dealer level is not, in our opinion, sufficient to support economically meaningful findings on this point.

[71] Finding 22.

cording to the Columbia Record Club's own figures, its profit on each record sold through the Club is not over 24¢ on those sold to first-year members, and not over 75¢ on sales to second-year members.[72]

The significance of the market share foreclosed by this cost disadvantage can be summarized as follows. Columbia produces in its own plants, as noted above, some 21.2% of all phonograph records bought by American consumers through all channels of distribution. And RCA and Capitol have an estimated 16% and 11.1%, respectively. Therefore, these three companies—Columbia, RCA, and Capitol—can foreclose from potential entrants into the club field some 48% of all records [73] simply by unilaterally refusing to sell their own respective labels (Columbia, RCA, and Capitol) directly to such potential entrants (or by refusing to sell except at prohibitively high prices). This still leaves, however, some 52% of the market "open" to nonintegrated clubs. Since both RCA and Capitol testified here that their clubs had been profitably operated with the use of only their own records—*i.e.*, RCA has operated a successful club using only RCA records (16% of all records sold in the country in 1960) and Capitol has operated a successful club

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[72] The price to first-year members, as noted, is an average of $2.37 per record. Subtracting the Club's average cost figure of $2.13 gives a per-record profit of 24¢. The second-year price averages $2.88; cost remains the same, $2.13, for a per-record profit of 75¢.

[73] Columbia did in fact refuse to sell to a club that attempted to enter except at the full wholesale-to-dealer price of $2.47, less periodic discounts, or an average price of $2.12. Tr. 9014–9015. A club paying that price for its records, and incurring the same additional costs that the Columbia Record Club incurs, would have total costs $3.37½, and hence would lose just over $1.00 on each record sold in competition with the Columbia Record Club at the latter's price of $2.37.

offering only Capitol records (11.1% of all records)—this remaining 52% would obviously be sufficient to permit the profitable operation of a number of additional record clubs besides those of the "big three." It is the foreclosure of the most significant portion of that nonintegrated 52% of the supply of records to potential club entrants, through the device of excluding them from direct access to these manufacturers, that is involved in the "licensing" contracts involved here. While data is not available on the share of all phonograph record sales through all channels of distribution by these nine manufacturers, a rough approximation is provided by Columbia's estimate of their share of all record sales through the largest of the distribution channels, sales through retail record dealers: [74]

Licensor Record Manufacturer	Date of Contract	Licensor's Share of Retail Dealer "LP" Sales in Year Prior to Contract	
		As % of all Dealer Record Sales	As % of all Dealer Record Sales
1. Caedmon	May 15, 1958		
2. Verve	March 31, 1959	0.6	1.1
3. Mercury	April 1, 1960	3.5	2.7
4. Warner Bros	September 15, 1960	1.5	1.4
5. Kapp	October 7, 1960	1.7	1.8
6. Vanguard	June 1, 1961	*	1.5
7. United Artists	July 1, 1961	1.6	1.1
8. Liberty	October 25, 1961	1.7	1.0
9. Cameo-Parkway	December 15, 1961	1.2	0.7
Total		11.8	11.3

* Indicates less than 0.5%.

No matter which of these figures is taken—11.8% or 11.3% of all record sales—the share of the nonintegrated supply effectively foreclosed by these contracts is substantial. Thus, 11.3% of *all* phonograph record sales constitutes some 22% of the 52% manu-

[74] RX 452 and 453, *in camera*.

factured by all firms *other than* the integrated "big three,"[75] and hence not subject to price control at the manufacturing level by those integrated competitors. In other words, the situation is one in which some 48% of the total supply of records is *already* controlled by the "big three" and hence subject to being withheld entirely from the new entrant into the "club" market (or sold to him only on terms so disadvantageous to him as to destroy his capacity to offer really effective competition), and in which one of those three integrated firms then proceeds to foreclose, by means of restrictive licensing agreements, economical access to *another* 11.3 percentage points, bringing the total record supply under the control of the big three to over 59% and leaving potential "club" entrants less than 42% from which to draw the records needed for club use.

25. The significance of the foreclosure is even greater to the would-be operator than any of these figures indicate, however. As noted above, not all of the approximately 25,000 separate records carried in the stores of the retail dealers are equally attractive to the particular segment of the record-buying public that joins phonograph record clubs. They tend to be relatively young, relatively unsophisticated in their record choices, and hence most prone to accept the most "popular" ("hit") records, those that are being played most frequently by the media and listened to most frequently by their friends.[76] The total quantity of records *suitable for club use* is therefore largely limited, as a practical matter, to the 100–400 records on the popularity "charts" at any given time. And the licensing agreements giving the Columbia Record Club exclusive club rights to the rec-

[75] 11.3% divided by 52% equals 21.7%.

[76] See Findings 19 and 20.

ords of these nine competitors cover a disproportionately large share of these "hits," *i.e.*, those licensor-competitors are particularly strong with the kind of artists (and hence of records) that appeal to the purchasers in the club market.[77] Thus, the March 24, 1962, popularity "chart" published by *Billboard* magazine (a trade magazine) listing the 150 largest-selling monaural LP's as of that date indicated that 33 of the 150, or 22% of them, were records produced by the licensor-manufacturers that have given the Columbia Record Club exclusive rights to their "club" sales.[78] Columbia itself had another 32 on that chart (21.3%), for a total of 65 (43.3%) of the "hits" on either Columbia or licensor labels. Columbia, RCA, and Capitol together accounted for 103 of those 140 best-sellers (69.3%).[79] The remaining 47 records

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[77] "[W]e have the artists whom the public wants to hear. If I may say so, I think that's an important point. A person who buys a record, popular or classical, is largely buying the record because of the particular artist's performance. In the pop field, if it's an Andy Williams or Johnny Mathis, they want what Johnny Mathis or Andy Williams will do. So it is in the classical field. They want Bernstein's performance of this work or Ormandy's of that, or Bruno Walter's, or whomever it happens to be. *The public is concerned with the artist* and that is, by the way, our complete philosophy of recording." Tr. 7324 (emphasis added). Thus, one of Columbia Record Club's advertisements declared that "every record checked on this page has hit the best-seller lists." CX 114.

[78] United Artists (7 best-sellers on the chart); Kapp (7); Cameo-Parkway (5); Mercury (4); Warner Brothers (3); Vanguard (2); Verve (1). CX 200.

[79] *Ibid.* It was of course precisely on the basis of its estimate of their capacity to produce future "hits" for its Club that Columbia signed up the nine licensor-competitors in the first place:

> The basic reason [for signing up Cameo-Parkway] was that . . . Columbia and the companies we were then affiliated with had not [had] a great deal of success with the teen-

(30.7%) constituted, for all practical purposes, the principal records available to potential club entrants for club distribution. A more realistic assessment of the share of the market covered by the contracts in issue here is thus made by comparing the 33 licensor-hits foreclosed to the potential club operator with the number that would have been available to him had there been no such contracts on that date, namely, 80, or 53.3% of the entire 150.[80] Those contracts thus foreclosed potential entrants into the club market from 33 out of a total of 80 (41.2%) best-selling records that would have otherwise been available (those not on the "big three's" own labels).

26. The significance of the "exclusive licensing" contracts described above lies, as noted, in the fact that they give Columbia a *price advantage* over any actual or potential competitor in the "club" market

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oriented type of material. We found the type of members we were getting in were asking for this material. The profile of our club was getting younger, and we felt that we had to meet their legitimate requests for this type of material. Bernie Lowe, who was then head of Cameo-Parkway, had had a *long history of success in creating teen-oriented material* and one of his artists, Chubby Checkers, created the dance craze, the twist. He had, in addition, other popular teen artists such as Bobby Rydell. We felt, after he approached us, that it would be mutually beneficial for us to distribute his catalog through the club. Tr. 5199–5200 [emphasis added].

Similar testimony was given in explanation of the other contracts. See tr. 5165 (Caedmon); 5166 (Verve); 5185 (Mercury); 5189–5190 (Kapp); 5195–5196 (United Artists); 5197–5198 (Warner Brothers); 5201 (Liberty); 5201–5202 (Vanguard).

[80] It has subsequently been reported in the trade press that another one of the big three, Capitol, has similarly been given "exclusive" rights to the club distribution of a number of other record manufacturers, thus presumably reducing still further the supply of records suitable for club distribution available to the potential entrant into the club market.

(and, indirectly, in the nonclub market as well). It is this cost differential that makes it virtually impossible for competing clubs to enter the club market and successfully match the prices at which Columbia, RCA and Capitol [81] resell to the consuming public. This differential is accomplished by (1) allowing Columbia to borrow the "master" for a "royalty" payment (17.8¢) on each individual record it manufactures from that "master." The sum of that royalty payment (17.8¢ per record), and the additional costs Columbia actually incurs in manufacturing the physical records from that "master" (42.8¢), plus advertising and other costs, is a total of 87.5¢, the aggregate cost respondent actually incurs in acquring the finished licensor records, whereas (2) Columbia's competitors are compelled to acquire those same records, if at all, through the more expensive route of buying them, *as retailers, from wholesale distributors,* (all clubs are admittedly "retailers," in that they sell directly to the consumer and do so in direct competition with the traditional retail record store), at the usual distributor-to-dealer price of $1.60 to $2.47. In other words, Columbia has gotten a lower price for itself and has gotten, along with it, an agreement from its suppliers that they won't give that lower price to any of Columbia's club competitors. The result is a cost barrier [82] to any would-be new entrants in the club

[81] As noted below, RCA and Capitol were negotiating with certain other independent manufacturer-competitors for similar "licensing" arrangements at the close of the record in this proceeding and one of them, Capitol, has subsequently been reported by the trade press as having actually entered into such arrangements.

[82] As emphasized above, these "exclusive" contracts do not physically prevent competing clubs from acquiring or reselling the records of these nine manufacturers; they simply make it much more *expensive* for them to do so. Thus, the records of

market and the insulation of the Columbia Record Club from the added competition they necessarily would bring.

27. The effects of these arrangements on potential entrants to the club market are illustrated by the experience of a firm that attempted to enter in 1958, the Diners' Record Club.[83] Founded by Mr. Bernard Solomon (who also has an ownership interest in several small record manufacturing companies, one of which is also in the music publishing business), the firm was initially able to buy records *directly* from apparently all of the various manufacturers, including both the big three (Columbia, RCA, and Capitol) and the major independents. According to the testimony of Mr. Solomon, some of the *manufacturers* had sold him records for as little as 50¢ per record, the more general price, however, being some $1.50.[84] Then, the manufacturers stopped selling to him *directly:*

> Q. Did there come a time during the operation of the Diners' Record Club when you were unable to buy certain products?

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any manufacturer in the country can be readily obtained in the "open market." *i.e.*, from that manufacturer's own *distributors* or from "transhipping" wholesalers who, in turn, acquire them from his distributors. Hence the only effect of these "licensing" provisions is to limit the *source* from which competing clubs can buy the records of these nine manufacturers, denying them the opportunity to buy *directly* from those manufacturers and therefore forcing all would-be competitors out into the "open market" where the price is necessarily higher. (As noted above, wholesale distributors *pay at least* $1.60 per record and hence must necessarily charge *at least* that amount to any club they might sell these records to.)

[83] This firm was not owned by the well-known Diners' Club but had a contract to use its name, mailing lists, etc.

[84] "Generally, it was $1.50 for monaural records and $1.75 for stereo records, but there were variations both ways where we paid a lot more in some cases." Tr. 3787. See also tr. 3817, 3844, 3907–3911, 3943, 6531.

A. Yes . . . Columbia, RCA and Capitol.

Q. Did there come a time when you were unable to buy [records] from Kapp Records [a Columbia licensor]?

A. Well, Kapp, I solicited and they said they couldn't sell me records.

Q. And did there come a time when you were unable to buy [records] directly from United Artists [another Columbia licensor]?

A. Well, I bought records from United Artists, but they discontinued selling the records to me.

Q. What is your understanding of the reason that Kapp Records discontinued selling to you? * * *

THE WITNESS: Well, Kapp Records never sold to me. We just had meetings, conversations, and correspondence, but they never sold me records. . . . Well, they *stated to me that they had an exclusive agreement with Columbia and couldn't sell me any records.*[85]

Q. What is your understanding of the reason United Artists discontinued selling to you? * * *

THE WITNESS: Mr. Si Mael and Harry Goldstein of United Artists both informed me that they had to stop selling me because of the arrangements with Columbia Record Club.[86]

Solomon had been selling, in his Diners' Record Club, a small label called "Challenge Records." Early in 1961, Warner Brothers, one of Columbia's "licensors," contracted with Challenge to take over its distribution. The Diners' Record Club promptly lost Challenge as a source of supply: ". . . Warners had an exclusive arrangement with the Columbia Record Club and they were taking over the distribution of Challenge: that could not be interfered with as part of the deal and Challenge would have to follow the same [ex-

[85] Tr. 3787–3788, 3790–3791 [emphasis added].

[86] Tr. 3790–3791.

clusive] route for clubs as Warner Brothers did." [87]

In reply to a direct request from the Diners' Record Club, David Kapp, president of Kapp Records, wrote Solomon as follows: "Our agreement with the Columbia Record Club is an exclusive one, and consequently we cannot enter into any agreement to sell you records for your club." [88] As to why the "big three" cut him off:

> Q. What is your understanding as to the reason the three majors [Columbia, RCA, and Capitol] refused to sell to the Diners' Record Club?
>
> THE WITNESS: In the cases of these approaches to these three companies, it was my understanding that the reason I couldn't buy product directly from the company was because of the existence of their own record clubs and therefore they didn't want to avail me of their products.[89]

Solomon explained the failure of his Diners' Record Club in these terms:

> Q. Mr. Solomon, why did your company go out of business?
>
> A. Well, as I said before; No. 1, a lack of adequate source of material of records to feature in the club. We had a basic repertoire from a number of companies, but we needed three major companies, certainly; Columbia, RCA, Capitol, as well as the affiliated [licensor] com-

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[87] Tr. 3796. While the Columbia-Warner contract covers only the distribution of certain specific Warner records, Solomon was still certain that he lost Challenge as a supplier because Columbia wanted it that way.

[88] CX 562. Similarly, Mercury wrote him, on January 27, 1961: "In view of our relationship with Columbia it is impossible for us to participate in your record club arrangements." CX 563.

[89] Tr. 3801–3802.

panies to Columbia Record Club in order to successfully operate the business.[90]

Columbia maintains that the Diners' Record Club went out of business because of the business inadequacies and personal shortcomings of its controlling stockholder and chief executive officer, Mr. Solomon. It is alleged that those manufacturers who have refused to sell to him have done so for reasons unrelated to the issues involved in this case, including such things as slowness in paying for records previously sold to him, allegedly unreasonable demands on his part for price and promotional concessions from his suppliers, and, apparently, for alleged discrepancies in his income tax reports. While the first two items are obviously relevant, the record suggests that the financial difficulties of Mr. Solomon's Club, and hence his problems with creditors and his efforts to get more favorable terms, were at least in a substantial measure related to the price disadvantage he worked under.

Respondent also suggests that, notwithstanding the licensing provisions prohibiting its nine licensor-competitors from selling to any other club, Solomon's Club was still able to get records from those manufacturers. There is some evidence that at least some of those companies did make a few sales to Diner's Rec-

[90] Tr. 3928. He testified further: "Let me say that a lot of the names and material that we did offer in the club, as Mr. Rabinowitz [Columbia's attorney] pointed out before, were good names; however, they must be recognized that these were old masters that were recorded many years ago, and the quality was inferior. These same artists had all since gone and been attracted to Columbia, RCA, Capitol and other larger record companies, and we were dealing with old-type product, even though they had a name stature they still didn't stand up to the performance—their current performance. In addition, a lot of this older catalogue was not in stereo and stereo was a very big factor in our operation." Tr. 3928–3929.

ord Club after having promised Columbia they wouldn't do so. For example, Solomon conceded that Mercury sold him some 100,000 records for about 50¢ per record not only after the date of Mercury's "exclusive" contract with Columbia but even after the January 27, 1961, letter explaining that its contract with Columbia made it impossible for Mercury to do business with him.[91] (These and later sales were apparently accomplished through the device of letting Solomon set up his own ostensibly "independent" distributorship.[92]) However, some 90% of the records bought at that price were what the industry calls "cutouts," records with so small a demand that the manufacturer is no longer currently producing them—in short, records that are on "sale."[93] The few current records they let him have "were put in in order to, like they call it, sweeten the pie."[94] Secondly, although Solomon was able to buy some records from Mercury still later through his own "distributor," he testified that "the prices were anywhere from 55 to 60 per cent higher than I had paid previously."[95]

28. A significant feature of these contracts giving the Columbia Record Club the sole and "exclusive" right to make copies of and sell these competitors' records in the club market is that, with two exceptions,[96] they gave Columbia the right to *prevent other*

[91] CX 563.

[92] Tr. 3944–3945.

[93] Tr. 3950–3951. Solomon defines them as records that "can be purchased on the open market at a price of less than a dollar and are not sold through the regular distributors, but through various . . . distress sale operations." *Ibid.*

[94] Tr. 3952.

[95] Tr. 3945.

[96] The Warner Brothers and Vanguard contracts covered certain named records of those two labels, rather than their entire catalogs. CX 39, 43.

clubs from using *even the records Columbia did not want to use itself*. The total number of records thus removed from club distribution by these licensing agreements was 1,773, or 70.7% of the 2,509 records owned by these 7 licensor-manufacturers in the 1962–63 period. Or, to put it another way, the Columbia Record Club elected to use 736, or 29.3% of those 2,509 records, and effectively precluded anyone else from using any of them, including not only the 29.3% it picked out for its own use, but the remaining 70.7% as well. This is shown for each of the licensor labels in the table below: [97]

Licensor-Mfr.	Number of Records in Catalog	Licensor Records Used by Columbia Club	
		Number	Percent of Total Number in Catalog
Caedmon	194	76	39.18
Verve	695	86	12.37
Mercury	754	279	37.00
Kapp	275	124	45.09
United Artists	283	68	24.00
Liberty	248	77	31.05
Cameo-Parkway	60	26	43.33

29. Entry into the business of manufacturing or producing phonograph records for sale through the conventional distributor-retailer channels is relatively

[97] The catalogs of these companies are included in the record as CX 265, 285, 289, 398, 445, 470 and RX 298. Respondent's officials initially testified that the Club had actually used 51 of Caedmon's records, 47 of Verve's, 177 of Mercury's, 86 of Kapp's, 54 of United Artists', 63 of Liberty's, 20 of Cameo-Parkway's. Tr. 5251–5252. Columbia's counsel, in oral argument before the examiner, said: "The Club has used almost 24% of United Artists catalog and not 17% as claimed at page 33 of Complaint Counsel's reply; and has used almost 37% and not 28% of the Mercury catalog." Tr. 11,074. And, by July 1963, the Club had used 26 Cameo-Parkway records, 43% of that label's catalog. *Ibid.*

inexpensive. Representatives of several producers testified that all the new entrant needs is an artist under contract and enough money to (a) rent a recording studio for the required number of hours and (b) hire a "custom presser" [98] to run off a few thousand copies of the record for distribution to the "disc jockeys" and wholesale distributors around the country. The "custom presser's" charge for producing a "normal run" of 10,000 finished records from a tape is, as noted, 38¢ per record,[99] or only $3,800. And while the cost of a contract with a well-known artist can run into many thousands of dollars, there is testimony here that there is no shortage of *new* artistic talent [100] and hence that the new entrant has no difficulty in "discovering" new artists at relatively modest costs. This is corroborated by the fact that some 20 firms have entered since 1945: [101]

Record Manufacturer:	*Year of Entry Into Record Industry*
RCA Victor	1928
Decca	1934
Columbia	1938
Capitol	1942
Mercury	1945
London	1946
Imperial	1946
Miller International (Stereo Fidelity)	1947
Jay-Gee (Jubilee)	1947
Atlantic	1948
MGM	1949

[98] Tr. 2827.

[99] Tr. 2832–2834.

[100] Tr. 5740–5746.

[101] RX 437. Interestingly enough, entry into record *retailing* appears to require considerably more capital than entry into record "manufacturing." Thus, whereas several producing firms were founded on initial investments of $5,000 or less (*e.g.*, Starday, tr. 5740–5746), one retailer testified that he had paid $80,000 for his business—$40,000 for his record inventory, $15,000 for fixtures, and $25,000 for the store's goodwill. Tr. 3157, 3161.

Record Manufacturer—Continued	Year of Entry Into Record Industry
Dot	1950
Vanguard	1950
Kapp	1953
Audio Fidelity	1954
ABC-Paramount	1955
Liberty	1955
Verve	1955
Cameo-Parkway	1956
Chess Record	1956
United Artists	1957
Roulette Records	1957
Warner Brothers	1958
Reprise Records	1961

30. Entry into the "club" or "subscription selling" mail order market, however, is more expensive. Columbia suggests that the capital requirements for entering the "club" market are very high, relying principally on the fact that its own Columbia Record Club was launched in 1955 with an advertising campaign that cost $500,000; that its own Club spent some $8 million on advertising in 1962 (15% of sales); that servicing the Club operation is very expensive; and that Diner's Record Club, attempting to enter on an initial capital of $5,000 and another $30,000 in initial advertising funds secured from suppliers, ultimately went out of business.[102] Respondent's economist, Mr. Peter Max, using the "net assets" held by Columbia, RCA, and Capitol when they formed their respective clubs in 1955 and 1958 ($48.9 million, $26.8 million, and $305.6 million, respectively) as a test of adequate financial resources for entry,[103] concluded

[102] Finding 27.

[103] "Now, I should explain very briefly the measure that I selected here, namely, current net assets. This, of course, is defined as—in terms of balance sheet accounting—as the company's current assets less its current liabilities. It therefore yields, as a residual amount, a measure of the company's *highly liquid* assets or liquid assets which are unencumbered by short-

that there were at least six (6) "potential entrants" capable of making a "serious entry into this area": [104]

Record Company:	*1961 Current Net Assets*
Decca (MCA, Inc.)	$63,954,386
London	18,055,842
Dot (Paramount Pictures)	75,118,096
MGM	90,943,354
ABC-Paramount	65,941,312
Colpix (Columbia Pictures)	44,178,523

Applying this test, however, at least three (3) others of the nine (9) "licensors" (besides MGM) are also potential entrants into the club business: [105]

Record Company:	*1961 Current Net Assets*
United Artists	$65,364,751
Warner Brothers	47,513,439
Mercury (Consolidated Electronics)	40,554,784

31. As to the number of firms that have actually entered the "club" market, respondent's economist testified as follows: "As we know, it was only in 1955 when Columbia, as the first full catalog club, entered or launched into the mail [order] method of distribution in a serious way. Since that time, of course, there have been some highly significant entrants. Obviously the entry of Capitol and the entry of RCA Victor into this channel of distribution constitute highly significant entries. In addition, in defining this channel of distribution as the purveying of records through the mail, we have entry of such entities as *Life* [magazine] in, I believe, 1962. Dot [Records], very recently, as I understand it, at least in a preliminary way; I believe the record indicates a similar sort of entry, at least in a preliminary way, by Starday [Records].

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term liabilities and represents in physical terms, of course, such things as cash and readily marketable securities which funds, if the company so chose, might be used to finance significant or serious entry into this area." Tr. 9789–9790 [emphasis added].

[104] Tr. 9789–9790; RX 487.

[105] *Moody's Industrial Manual*, 1963.

Apart from RCA Victor, we have the entry into the distribution of records by mail by *Reader's Digest* [magazine] in fairly recent years."[106]

In fact, only three (3) of these—Columbia, RCA, and Capitol—are "serious" or "significant" factors in the club market. Starday, a small manufacturer of records located in Madison, Tennessee, a suburb of Nashville, started producing records in 1952 on a beginning capital of less than $1,000 and had total sales of only $600,000 in 1962,[107] a very small fraction of 1% of the industry's 1962 sales. As to its own club: "I hope to start my own record club because I recognize the need. Whether I would want Columbia or one of the other clubs to handle my records would depend on unforeseen things in the future pertaining to my own club, if I get it started."[108]

We know of no record evidence of any club having been in fact started by Dot.[109]

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[106] Tr. 9788.

[107] Tr. 5755.

[108] Tr. 5764.

[109] Mr. Randolph C. Wood, President of Dot Recording Corporation and Vice President of his parent company, Paramount Pictures, testified that, from the selling of appliances in Gallatin, Tennessee, he had "entered the mail order business [of] selling records by mail, COD by radio" in 1947, and had founded Dot Recording Corporation in April of 1950. Tr. 4103. He testified further:

> Q. Are you presently interested in having your products sold through a record club?
>
> A. Mr. Lavine, I have been interested for several years, to the point of constantly thinking about this facet of the business, because in order to be competitive and do the best job for our artists, which, after all, are the most important part of our operation if you had to narrow it down, for competitive reasons I am almost *forced* to be interested in club operation, either through affiliation or through our

32. There has been no successful entry into the "club" market,[110] then—at least as far as this trial record indicates[111] since RCA and Capitol entered in 1958. One serious attempt at entry was made, and it

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own club. That doesn't mean that I really want to do it. It is the fact that I feel that I will have to do it or should do it.

Q. Are you taking steps at the present time to implement this point of view?

A. We are contemplating [it] but [have made] no definite decision. We are running mail order tests and we have negotiated and discussed the possibility with all of the companies who have clubs in the past; so far, we have not made a definite decision.

Q. When you say you are running mail order tests, is that with a view to the possibility of starting a Dot Record Club?

A. Yes, it would be a Dot Record Club. (Tr. 4119–4120; emphasis added.)

Organized on an original investment of about $1,000, Dot records had sales of some $15 million in 1962 (tr. 4127–4135), mail order sales of less than $100,000. It had, over-all, some 3.6% of the dealer LP market in 1961. CX 241.

[110] There is, as discussed in Finding 15, no serious competition between "club" and "package" records.

[111] The trade press has subsequently reported, and advertisements confirm, the entry of a firm called "Record Club of America." Neither complaint counsel nor respondent have offered to inform us as to the competitive significance of this new entrant. It recently filed a motion to intervene in this proceeding, but only for the purpose of advising us that Capitol, like Columbia, had entered into a series of "licensing" agreements with other manufacturers, thus acquiring exclusive club rights over those manufacturers' records and denying the movant access to them. That information was largely cumulative of what was already in this record, and the motion to intervene was accordingly denied. Since both complaint counsel and respondent requested that the Commission deny that motion to intervene, we assume they are agreed that this new entrant, Record Club of America, has no competitive significance in the club market.

failed largely because of the cost disadvantage it suffered under in acquiring records for resale through its club. The club market thus remains, after nearly 10 years since the last of the "big three" entered a tight knit oligopoly, with a single firm, Columbia, holding more than 50% of the market and two others, RCA and Capitol, sharing the bulk of the other 50%. This is in marked contrast to the relatively high rate of entry into the producing of phonograph records and clearly suggests the presence of substantial barriers to entry. The most formidable is plainly the "exclusive" licensing contracts between the Columbia Record Club and its nine licensor-manufacturers, and the 71.5¢ or more per record cost disadvantage [112] they impose on potential entrants into the club business on the records of this group of major independent producers, producers whose records a potential entrant would want to sell in a new club operation. This cost barrier constitutes a serious impediment to entry into the club market,[113] and the cause of a substantial lessening and prevention of competition within that market.

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[112] Findings 6 and 22.

[113] We reject as frivolous the contention of respondent's economist, Mr. Peter Max, that these nine (9) "exclusive" licensing contracts, wherein those firms expressly promise not to start their own club and not to sell to anyone else who starts a club, constitute a "form of entry." Tr. 9791–9793. The essence of the concept of entry is the addition of a new decision-maker to challenge the price and product policies of the established firms and put competitive restraints on their discretionary power. See, *e.g.*, Joe S. Bain, *Barriers to New Competition* 5 (1956). Here, these nine (9) firms, all potential entrants themselves and producers of products needed by other entrants expressly abdicated that vital decision-making function, appointing the Columbia Record Club, in effect, their exclusive sales agent, to make all "club" decisions for them.

CONCLUSIONS

1. The Columbia Broadcasting System, Inc., and the Columbia Record Club, Inc., are corporations engaged in commerce, as "commerce" is defined in the Federal Trade Commission Act.

2. Respondent has entered into a series of "exclusive licensing" contracts with nine (9) of its competing phonograph record manufacturers or producers whereby, in return for "royalty" payments that average approximately 17.8¢ per record, those producers loan or "license" their record "masters" (from which finished records are made) to the Columbia Record Club on an "exclusive" basis, agreeing, in substance, that for a period of years they will not (a) sell their records through a mail order "club" operation of their own; (b) sell their records directly to anyone else who resells through a mail order "club" operation; or (c) allow anyone else to use their "master" recordings for the purpose of producing finished records for resale through a mail order "club" operation.

3. The relevant market in which to evaluate the competitive effects of these licensing agreements is the sale of phonograph records through mail order record "clubs." Members of such clubs constitute a separate and distinct sector of the record-buying public, their distinguishing characteristics being (a) a relatively high propensity to shop by mail, (b) a relatively high or beginner's interest in securing "guidance" or expert assistance in selecting records for that collection, and (c) a relatively active interest in buying at economical prices. The individuals that make up this market tend to be relatively young adults that have just purchased a phonograph record player, and that are interested in having someone else select for them the most "popular" or "hit" records at lower prices than can be secured in the conventional record deal-

ers' stores. The clubs of the "big three" record producers (Columbia, RCA, and Capitol) cater to this distinct group of customers by selling them a limited variety of "hits" (some 200–400 per month, versus the 25,000 available in dealer stores) at a price that is approximately 20% lower than the dealers charge for the same records ($2.37 versus approximately $2.98). The clubs are able to sell to this market at these prices because they enjoy substantially lower costs than the nonclub retail dealers. Different prices and different costs in the two channels of distribution clearly indicate that different conditions of supply and demand prevail in each and that they therefore belong to separate and distinct "markets."

4. The purpose and the effect of these exclusive licensing contracts is to prevent other actual or potential club operators from acquiring the records of those nine producers on equally favorable terms. Because of those agreements, other clubs cannot buy at all from these manufacturers themselves, nor can they "rent" the latters' "masters" and fabricate their own copies as the Columbia Record Club is allowed to do. Rather, the existence of these exclusive grants to Columbia forces other clubs desiring to sell the records of those nine producers to go to the latters' wholesalers and pay $1.60 or more per record—as contrasted with the 87.5¢ the same records (Mercury, Kapp, Warner Bros., etc.) cost the Columbia Record Club. This cost disadvantage has the effect of barring potential newcomers that would otherwise have found the operation of a club profitable and hence of preventing competition with the clubs of the "big three" that could have otherwise been reasonably expected to flourish. The result is that a competitive industry structure has never been allowed to develop in that market. The Columbia Record Club had 56.1% of that

market in 1960; RCA had 26.8%; and Capitol had 7.7.% Together, the clubs of the "big three" controlled 90.6% of all phonograph record sales through clubs. As a result, potential competitors (clubs) have been denied access to that market and the returns they could have otherwise have earned in it and the public has been denied the lower prices and other benefits that could reasonably have been expected to flow from the heightened competition their entry would have created. This prevention of competition constitutes an unfair practice and an unfair method of competition within the meaning of Section 5 of the Federal Trade Commission Act.

5. Respondent has further fixed and continues to fix and maintain, by agreement with several competing manufacturers or producers of phonograph records, the prices (royalties) paid by those producers, to the artists who record for them on records sold through the Columbia Record Club, in violation of Section 5 of the Federal Trade Commission Act.

ORDER

IT IS ORDERED that respondents Columbia Broadcasting System, Inc., and Columbia Record Club, Inc., and their officers, representatives, agents and employees, successors, or assigns, directly or indirectly, or through any corporate or other device, in connection with the manufacture, promotion, offering for sale, sale and distribution of phonograph records in commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

Entering into, maintaining, or continuing any contract, licensing agreement, or understanding with any other manufacturer or producer of phonograph records to:

(a) Establish, fix, or maintain the price or royalty paid by any other manufacturer or producer of phonograph records to any artist for such artist's recording services;

(b) Prevent other club operators, including potential club operators, from acquiring the phonograph records of any other manufacturer or producer on the same terms and conditions as respondents acquire such records, including but not limited to agreements which have the effect of:

i. Giving respondents the sole or exclusive right, privilege, or license to manufacture, distribute or sell through clubs phonograph records manufactured from master recordings owned or controlled by any other manufacturer or producer of phonograph records;

ii. Restricting or preventing any manufacturer or producer of phonograph records from licensing, authorizing, or consenting to the making of phonograph records from its master records by any other person for the purpose of resale by the subscription or club method of direct mail selling;

iii. Restricting or preventing any manufacturer or producer of phonograph records from selling its own records by the subscription or club method of direct mail selling;

iv. Restricting or preventing any manufacturer or producer of phonograph records from selling its records directly to any person for resale by the subscription or club method of direct mail selling.

IT IS FURTHER ORDERED that the initial decision be, and it hereby is, set aside, and the Findings As To the Facts, Conclusions and Order of the Commission be, and they hereby are, substituted therefor.

IT IS FURTHER ORDERED that respondent shall, within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting

forth in detail the manner and form in which they have complied with the order set forth herein.

By the Commission, Commissioner Elman not concurring.

[SEAL] JOSEPH W. SHEA,
Secretary.

ISSUED: July 25, 1967.

OPINION OF THE COMMISSION

By DIXON, *Commissioner:*

The complaint in this case, issued on June 25, 1962, charged that the Columbia Broadcasting System, Inc., and its wholly owned subsidiary, Columbia Record Club, Inc., had engaged in certain unfair business practices in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45,[114] including attempted monopolization, the "squeezing" of retail dealers with whom it competes, and the making of agreements with competing record manufacturers to fix noncompetitive record prices, fix and depress the prices paid to artists for their recording services (royalties), and cut off the supply of certain records to actual and potential competitors in the "club" sector of the phonograph record industry.[115] Hearings were held before a hearing examiner of the Commission, and approximately 11,000 pages of testimony and 1,400 exhibits in support of and in opposition to the allegations of the complaint were received into the record. In an initial decision of 304 pages filed

[114] That section provides in part: "Unfair methods of competition in [interstate] commerce, and unfair or deceptive acts or practices in commerce, are hereby declared unlawful."

[115] The complaint also charged (Count II) that respondents had unfairly misrepresented, in certain of their advertising, the "savings" to be realized by the consumer in purchasing records from the Club. That charge was subsequently abandoned by counsel supporting the complaint.

September 30, 1964, the examiner found that the allegations of the complaint had not been sustained by the evidence and ordered the dismissal of the proceeding.

We believe that decision was erroneous and hence must be reversed and set aside.

The charges in the complaint center around Columbia's formation and operation of its Columbia Record Club, an organization that distributes phonograph records direct to the consuming public through what is called the "club" or "subscription" form of mail order selling.[116]

Columbia entered the club market in August of 1955. One of its purposes in so doing was to prevent the entry of certain nonrecord firms, particularly the entry of mail order book-distributing organizations.[117]

Commencing in May 1958, Columbia decided that the Club could be more profitably operated if it sold not just its own (Columbia) records, but those of some of its competitors as well. However, instead of going to those manufacturers' wholesale distributors (the "open market") and buying the records at the same price paid by other record retailers (the Columbia Record Club is admittedly a "retailer," in that it sells directly to the ultimate consumer), the Club entered into a series of "licensing" agreements with nine (9) of its medium-sized and smaller competitors under which it gets their records for a total of some 87.5¢, versus a price of $1.60 or more all competing retailers are required to pay for those same records. It also included in those "licensing" agreements provisions (a) fixing (depressing) the price (royalty) to be paid by those manufacturers to their artists on records sold through

[116] Finding 3.

[117] Finding 5.

the Columbia Record Club,[118] and (b) giving the Columbia Record Club the sole and "exclusive" right or "license" to make records from those nine competitors' "master"[119] recordings (for a "royalty" of some 17.8¢ per record made from them), those competitors expressly promising not to engage in a club operation themselves, not to sell directly to anyone else who operates a club, and not to allow anyone else to use their "masters" for the purpose of producing records to be sold through a club. In short, Columbia sought to assure itself that no one else would be able to sell the records of those nine producers through the mail in competition with the Columbia Record Club.

I

The Columbia Broadcasting System, Inc. (hereinafter CBS or Columbia) is a New York corporation with seven (7) operating divisions, one of which is Columbia Records,[120] a manufacturer and seller of phonograph records. In 1961, CBS as a whole had sales of $473.8 million and net assets of $142.4 million. In 1961 and 1962, the Columbia Record Club had

[118] Two of the earlier contracts also contained provisions fixing the price at which the Columbia Record Club was to sell the competitors' records through the Club and fixing the price at which the competitors themselves were to sell the same records to their own distributors (nonclub channel). There is insufficient evidence to establish that those agreements are currently in effect, however, or that similar agreements were ever entered into with the other seven licensor-competitors. The evidence on the fixing of artists' royalties, on the other hand, is clearly set out in several of the contracts, including the later ones. Findings 10 and 11.

[119] A master is an original recording or duplicate thereof, from which other phonograph records can be manufactured.

[120] The other six are: (1) CBS Television Network, (2) CBS Television Stations, (3) CBS Radio, (4) CBS Laboratories, (5) CBS International, and (6) CBS News.

phonograph record sales of $41.5 million and $53 million, respectively; the company's nonclub sales of records (to wholesalers and retailers) was roughly the same in volume, making phonograph records somewhat less than 20% of CBS' total sales.

Columbia is the leading producer and seller of phonograph records in the United States. In 1960, total consumer expenditures for all kinds of records (including "LP's" and "singles" [121]), through all channels of distribution (including clubs, racks,[122] juke boxes, and dealer stores), was an estimated $521 million.

One of the principal issues to be determined in this proceeding is the "relevant market" in which the competitive effects of these challenged agreements with Columbia's nine competitors are to be evaluated. Respondent argues in favor of a broad "all-record" market. Counsel supporting the complaint, on the other hand, argues that the appropriate "relevant market" involved here is not the sale of all records through all channels of distribution but the sale of "LP" records only, through only one of the mail order channels, a method of selling by mail called the subscription of "club" technique.

The outer boundary of the relevant market is the broad, all-record market. This market, however, consists of four channels by which records are distributed to consumers: retail stores, racks, nonclub mail, and

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[121] "LP's" are the "long-playing," larger discs that have six performances on each side and retail for $2 and up; "singles" are the smaller discs with one performance on each side, retailing for less than $1. The LP's account for about 75% of all record sales, "singles" for the remaining 25%.

[122] "Racks" are the familiar structures displaying the 50 or so current "hits" in supermarkets, drug stores, and other high traffic areas.

club mail.[123] We find the club market to be a relevant submarket.

The very fact of these agreements excluding competitors from an equal opportunity to sell these records "through any mail order record club" [124] evidences Columbia's *own* conviction that the clubs are a sufficiently distinct market to make this restrictive arrangement economically worthwhile. As one text writer has put it, "the courts will take as the market, for the purposes of deciding cases, just that market which the concern itself takes for its field of activity; if a firm shows an intent to exclude competition from that field, it will be assumed that the field sufficiently describes a market, for otherwise what would be the point of the effort to exclude?" [125]

Furthermore, as discussed in some detail in the accompanying Findings As To The Facts, a number of economic factors operate to produce entirely different conditions of supply and demand in the sale of phonograph records through the various submarkets. Each of the relevant submarkets possesses different cost components and structures.[126] On the demand side they offer consumers different sets of advantages and disadvantages. The clubs especially appeal to a group of customers that have certain distinctive characteristics.[127] These supply and demand conditions are sufficiently different between the retail and club markets, for example, that each is capable of generating particular competitive forces which, in turn, can discipline one another.

The present arrangement is found to be a restriction upon competition in the club market as a relevant sub-

[123] Finding 13.
[124] CX 20.
[125] Neale, *The Antitrust Laws of the USA*, p. 125 (1960).
[126] Finding 22.
[127] Findings 19 and 20.

market. In addition, this practice lessens the competitive contribution of the club submarket to the broader, all-record market. In certain structural situations a given practice which occurs and is measured in a relevant submarket can have an adverse effect not only in that submarket but also upon the broader market itself. This is especially true—as in the instant case—where the submarket under question enjoys a cost advantage.[128] The capacity of the other channels of distribution to discipline the club sector is limited by their cost disadvantages. In such an instance it is especially important to maintain the level of competition in the advantaged outlet.

II

Columbia maintains that the "licensing" agreements challenged in this proceeding were entered into with its nine competitors for the purpose of meeting the demands of its Club members for a greater "variety" of records to choose from. The evidence is very clear, however, that the relatively small number of records offered by the Columbia Record Club is not a matter of record shortage but a deliberate policy on the part of the Club's officials, in accordance with what they conceive to be the particular tastes of their Club members. The Columbia Record Club could offer an unlimited variety of phonograph records to its members if it thought such a policy would be more profitable than the narrower selection it now offers.[129]

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[128] Findings 22 through 24. For a brief discussion of the significance of different cost structures upon competition among relevant submarkets (or "interindustry competition") see: (1) Kaysen and Turner, *Antitrust Policy*, p. 102, fn. 2 (1959) and (2) *United States* v. *Corn Products Refining Co.*, 234 Fed. 964, 975–977, (S.D.N.Y. 1916).

[129] See Findings 21, 25 and 28.

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The purposes and the effects of the "licensing" agreements at issue here are twofold, namely, (a) to give the Columbia Record Club a discriminatorily low price on the "hit" records of those nine competitors, and (b) to bar the entry of competing clubs into the market by denying them access to suitable records ("hits") on equally favorable terms, *i.e.*, at costs that would permit them to profitably compete with the Columbia Record Club.

It should be emphasized that, while these agreements are couched in terms of "exclusive" contracts, their immediate effect is not to deny other club operators access to those records altogether, but simply to make the newcomer pay a higher price for them. Thus, it was agreed between Mercury Records, one of the nine "licensors," and the Columbia Record Club, that "during the term of this agreement you [Mercury Records] will not, in the territory of the United States and Canada, (1) sell by direct mail, (2) offer for sale by direct mail, or (3) authorize or consent to the sale or offering for sale by direct mail by any third party of phonograph records manufactured from master recordings which you now own or control or which you may hereafter own or control." [130] The effect of this provision is not, however, to physically prevent other clubs from acquiring these records at all; rather, since anyone can buy any manufacturer's records on an "open market" at a going market price from the country's hundreds of independent wholesalers,[131] the effect is simply to force any other club

[130] CX 34, p. 3, par. 7.

[131] These nine competitors of Columbia promised only that *they* would not sell to any other club operator and wouldn't "authorize or consent" to the sale of their records through a club by any third party. There is of course no authority under the law for these manufacturers to control the further disposi-

desiring to sell those records to go to the wholesalers and pay that "open market" (distributor-to-dealer) price of $1.60 to $2.47.[132] Under these licensing agreements, however, the Columbia Record Club's total costs of acquiring a finished Mercury, Kapp, or other licensor record, ready for sale through the club, is 87.5¢.[133] This gives it, then, a cost advantage on these records of from 72.5¢ to $1.59½, depending on whether the new club operator is able to acquire those same records from the wholesalers at the "best" price ($1.60) or the "list" price ($2.47). The magnitude of this barrier[134] thus thrown up in the path of potential club operators is suggested by the fact that the Columbia Record Club's own profit, according to its own figures, was no more than 24¢ per record on sales to first-year members and 75¢ per record on sales to second-year members.[135]

This cost "handicap" imposed on potential club entrants by these licensing agreements has obviously affected the structure of the club market and seriously

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tion of their records, once those records have been sold to their wholesalers, *i.e.*, the producers cannot lawfully prevent their wholesalers from reselling the records to other clubs, regardless of what the "exclusive" contracts with Columbia might say about it.

[132] Finding 23.

[133] Finding 22.

[134] Barriers to entry are "evaluated roughly *by the advantages of established sellers in an industry over potential entrant sellers.* . . ." Bain, *Barriers to New Competition* 3 (1956) (emphasis in original). One such barrier is the ability of established firms to secure needed input factors, *e.g.*, phonograph records for resale, "at lower prices than potential entrants can. . . ." *Id.*, at 14.

[135] The Columbia Record Club reported total costs of not less than $2.13 per record. Subtracting this from its first- and second-year prices of $2.37 and $2.88 gives a profit of 24¢ and 75¢, respectively.

lessened the vigor of competition in it. There can be little question but that entry into that market would be substantially more attractive if the potential entrant could secure the records of these nine manufacturers for the 87.5¢ paid by the Columbia Record Club, rather than for the $1.60 to $2.47 charged by the wholesalers. The records of these nine firms constitute a quite substantial share of the total supply of records available to club operators on at least potentially realistic terms. As discussed in the accompanying Findings, the "big three"—Columbia, RCA, and Capitol—can foreclose from potential entrants into the club field some 48% of all records simply by unilaterally refusing to sell their own respective labels (Columbia, RCA, and Capitol) directly to such potential entrants (or by refusing to sell to him except on prohibitive terms.)[136] For all practical purposes, then, the new club that expects to seriously compete with the clubs of the "big three" would be limited to the records of the nonbig three manufacturers, those represented by the remaining 52%.

Since RCA and Capitol both testified in this proceeding that their clubs had been profitably operated with the use of only their own records—*i.e.*, RCA has operated a successful club using only RCA records (16% of all records sold in the country in 1960), and Capitol has operated a successful club offering only Capitol records (11.1% of all records)—this remain-

[136] Columbia did in fact refuse to sell to one ultimately unsuccessful club except at the full wholesaler-to-dealer "list" price of $2.47, less periodic discounts, or at an average price of $2.12. Tr. 9014–9015; finding 27. A club paying that price for its records, and incurring the same additional costs that the Columbia Record Club incurs, would have total costs of $3.37½, and hence would lose just over $1 on each record sold in competition with the Columbia Record Club at the latter's price of $2.37.

ing 52% would undoubtedly be sufficient to permit the profitable operation of a number of additional record clubs besides those of the "big three." The "licensing" contracts involved here, however, not only expressly bar these nine most likely entrants from starting their own clubs,[137] but dries up their share of that remaining 52% of the total supply of records to all other potential entrants. They sold, in the 12 months prior to the signing of their respective licensing contracts with Columbia, an aggregate of some 11.2% of the LP's [138] sold through retail dealer stores.[139] This transfer of another 11.2 percentage points out of the nonintegrated sector and over to one of the "big three" integrated firms further reduces by that amount the supply of records available to potential new club operators on economical terms.

The foreclosure involved here, however, is considerably greater than that indicated by any of these figures. As noted above, not all of the approximately 25,000 separate records offered for sale by the country's approximately 50 record manufacturers are equally attractive to the particular segment of the record-buying public that joins clubs. Their preferences run primarily to the most popular of the "hit" records, particularly to the 150 or so records that are, at any given moment, on the popularity "charts" published by the trade magazines (*Billboard*, etc.). It is from these much smaller groups of records that the bulk of the records *suitable for club use* are apparently drawn in actual practice. And of course it was precisely on the basis of their actual or potential ca-

[137] Findings 6–9.

[138] "Singles" cannot be sold economically through clubs.

[139] This is presumably a fair approximation also of their share of all LP sales through all nonclub channels of distribution, *i.e.*, racks and juke boxes as well as dealer stores.

pacity for producing "hits" that the nine "licensors" were selected by Columbia in the first place.[140]

These licensing contracts foreclosed to potential club entrants (except on disadvantageous terms) some 41.2% of what would otherwise have been an "open" market in "hit" records suitable for club use.[141]

But even if the effects of these contracts are evaluated not in terms of the share of club-type records actually tied up by the Columbia Record Club and hence actually foreclosed to potential club operators, but simply in terms of the smaller dollar share represented by the Columbia Record Club's *sales* of those particular records it ultimately elected to use itself (approximately 30% of the records it tied up), the principal conclusion would still be the same.

The Club's 1961 sales of $41.5 million were an estimated 53% of all "club" sales in that year, with approximately 36.7 percentage points representing its sale of its own (Columbia) records ($28.7 million), and the other 16.3 percentage points ($12.8 million) representing its sale of the nine competitors' records. In these circumstances we think the most clearly appropriate legal standards by which to judge the legality of the conduct involved are those expressed in the Supreme Court's recent merger[142] decisions,

[140] Finding 25.

[141] *Ibid.*

[142] While combinations effected by contract are admittedly less "permanent" than mergers of stock and all physical assets, we do not understand the law to be that competition may be lessened and monopoly created merely because it is scheduled to end at some specified future date: if there is injury to competition, there is injury to the public and should be ended without delay. Here, moreover, the time limit itself is more apparent than real: the contracts run for a stated period of years (*e.g.*, three years), but they are frequently renewed for additional periods of similar length.

It might be suggested that, since the actual effect of these

particularly those involving the so-called "horizontal" combinations.[143] The factual situation before us—one in which a firm with some 36.7% of the relevant market already, has acquired by contract with nine of its competitors another 16.3%, and in which it then shares over 90% of that market with only two other firms[144]—falls squarely within the rule of *Philadelphia Nat'l Bank* against a consolidation that "produces a firm controlling an undue percentage share of the relevant market, and results in a significant

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agreements is not to "exclude" competitors from access to the records of these nine licensors in the physical sense of that term but only to make them pay a higher price than the Columbia Record Club pays, the applicable legal standard should be that expressed in the price discrimination law. Since the price differential (87.5¢ vs. $1.60) has allowed into the club market no significant competitors other than the integrated "big three" and has thus given the Columbia Record Club a virtual monopoly on the sale of the records of these nine firms through clubs, we think the situation should be evaluated primarily in terms of merger standards. However, considering the magnitude of the discriminatory price involved (a discrimination of some 54.7% in the Columbia Record Club's favor) and of the market share it has been able to get and hold as a result of it (53% in 1962), the conclusion would doubtless be the same under the price discrimination law. *Utah Pie Co.* v. *Continental Baking Co.*, —— U.S. —— (April 24, 1967).

[143] *Brown Shoe Co.* v. *United States*, 370 U.S. 294 (1962); *United States* v. *Philadelphia Nat'l Bank*, 374 U.S. 321 (1963); *United States* v. *First Nat'l Bank & Trust Co.*, 376 U.S. 651 (1964); *United States* v. *El Paso Natural Gas Co.*, 376 U.S. 651 (1964); *United States* v. *Continental Can Co.*, 378 U.S. 441 (1964); *United States* v. *Aluminum Co. of America* (*Alcoa-Rome*), 377 U.S. 271 (1964); *United States* v. *Pabst Brewing Co.*, 384 U.S. 546 (1966); *United States* v. *Von's Grocery Co.*, 384 U.S. 270 (1966).

[144] See generally *Federal Trade Commission* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967); Brodley, "Oligopoly Power Under the Sherman and Clayton Acts—From Economic Theory to Legal Policy," 19 *Stanford L. Rev.* 285, 299 (January 1967).

increase in the concentration of firms in that market. . . ." [145] That merger, had it been allowed, would have produced a firm with 36% of the relevant market, substantially less than the 53% held here by the Columbia Record Club.

IV

Columbia offers several "business justifications" as to why it should be allowed to retain its "exclusive" hold on the sale of the records of these nine competitors in the club market. One of them—the argument that the Columbia Record Club is a less efficient retailer of records than the country's approximately 5,000 record dealers and thus should be allowed to buy at a lower price in order to offset the latter's alleged cost advantages—would be relevant only if the question was solely one of discrimination against, and competitive injury to, the dealers. Here, however, the competitive injury we find has occurred in the club rather than the nonclub market. A club's "justification" for inducing a discriminatory price not accorded to the operators of dealer stores obviously is no "justification" for contract provisions imposing a higher price *on clubs*.

Respondent argues further, however, that the Columbia Record Club is entitled to keep its "exclusive" hold on the Club sale of these records, and hence its advantage over other clubs, because of certain "guarantees" it gave the nine competitors in question. In negotiating these contracts, Columbia expanded its obligation beyond the unit "royalty" payment of so much for each licensor record sold (an average of 17.8¢ per record) by adding a promise on its part to pay the licensor-competitors a *minimum* total dol-

[145] *United States* v. *Philadelphia Nat'l Bank*, 374 U.S. 321, 363 (1963).

lar figure, regardless of how few licensor records the club might in fact sell. For example, in its contract with Kapp respondent agreed to pay Kapp royalties on *at least* 150,000 records per year, for four years.[146] From this point, respondent reasons as follows: "[T]hese [licensor] companies almost universally demanded guarantees and we felt that we could meet the guarantees more successfully if we had exclusivity on the artists and the product [records] produced by these companies."[147]

There would seem to be no question but that the Columbia Record Club could, in fact, "meet the guarantees *more successfully* if we had exclusivity" on those records, *i.e.*, that it could take in more revenue if it had a monopoly on the mail order distribution of those records than if it had to compete with others selling those same records through the mail. This follows from the elementary economic principle that the sale of any product is more profitable, *i.e.*, that more money can be gotten for it, if it is sold in a monopolized rather than a competitive market. It does not follow, however, that one can first agree to pay a high price for something, a price that reflects the expectation of being able to resell it in a market free of competition, and then use the high price originally paid for it as "justification" for keeping the monopoly. This is a circular or "boot-strap" argument, to say the least. Assuming that Columbia has in fact "guaranteed" to pay Kapp and the others more than the club can earn from the sale of their records in a genuinely competitive market,[148] this establishes only

[146] See CX 41, 44, 45, 81, 180, 184, 191, 265, 512.

[147] Tr. 5240.

[148] There is little evidence that the "guarantees" given are actually all that "high." Thanks to the "negative option" system employed by the Club, approximately 35% of the Club's total membership (some 2 million) can be expected to accept

that the parties knowingly bargained for the purchase and sale of a monopoly, not that the monopoly itself should be sustained. We know of no principle of law under which a private interest in realizing the fruits of a purchased monopoly must be given precedence over the public interest in preventing such monopolies.

Respondent's "advertising" argument is somewhat similar to those already discussed. A Club official explained it to the hearing examiner this way: "The basic reason [for demanding "exclusive" rights to sell these records through the mail] was that we would be advertising the artists and the labels extensively, spending millions on dollars in advertising for new members and in promoting these artists and their records and the labels in our club magazines, and we felt that during the period of the contract our [advertising] investment justified this exclusivity." [149] As we understand it, respondent's basic argument here is

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the record "selected" for them (the "regular selection") each month (Finding 3). Thus, in 1962, no "regular selection" in the Club's "popular division" (40% of the total membership) sold less than 95,000 records. In effect, this means that the Columbia Record Club can generally meet a 100,000–150,000 "guarantee" by simply picking *one* of the licensor's records for the coveted role of "regular selection" of the month. In fact, there is reason to believe this is the real significance of the guarantee provisions in the contracts—they assure the licensor he'll get at least one of his records featured as a "regular selection" and hence in the hands of 100,000 "automatic" buyers.

[149] Tr. 5239 [emphasis added]. Although Columbia's licensing contracts give it an "exclusive" on *all* of the records in each licensor's catalog (including new ones as they're released), it doesn't actually use all of them. Thus, of the 2,509 records offered for sale by these nine producers, the Columbia Record Club has elected to use or offer to Club members only 736 (29.3%) of them. Its "exclusive" contracts, however, barred all other clubs from using not only these 736 records but the other 1,773 records (70.7%) as well, records that it had no

that its advertisements, some of which carry the names of these nine licensor-competitors' labels, and the names and pictures of some of their more popular artists, have created some sort of residual or continuing "demand" for the records of those manufacturers and their artists and that this continuing "demand" is something respondent alone, as its creator, should be allowed to exploit. To allow a newcomer to sell Mercury, Liberty, Verve, Caedmon, Kapp, Warner Bros., United Artists, Vanguard, and Cameo-Parkway records through the mail would thus permit such a newcomer to take a part of what respondent's advertising had created—in short, it would, as we understand the reasoning, permit him to reap where he had never sowed. Or, stated another way, respondent is apparently arguing for the establishment of a principle of law that the *first* seller to *advertise* a given product must thenceforth be allowed to enjoy a monopoly on the sale of that product in the area covered by his advertisement, lest some residual "demand" created but not harvested by that first advertiser be

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desire to use itself but didn't want anyone else to use, either. The President of RCA testified that, in his view, this was one of the "deleterious" effects of exclusive licensing: "[N]o record club can use up all of the repertoire of a Verve, a United Artists, other labels, and that it may well be, if you have an exclusive contract with another label, that part of the repertoire remains unused: it lies fallow: it stays on the shelf. And if that is true, then the cultural effect, as you call it, would be deleterious." Tr. 1871. He also thought it had bad "commercial" effect: "I think exclusive [licensing] contracts, in that sense, such as the one that Columbia has had with [these licensor] labels, [is] likely to have certain bad effects. These bad effects . . . always do come about when one agency in distribution or in entertainment, becomes so all-powerful [a] smaller manufacturer listens all too carefully to what this agency dictates or tells [it]." Tr. 1871.

garnered by later entrants into that market. We are at a loss to understand how, under such a rule as this, competition could ever arise at all.

There is nothing in respondent's advertisements to support such a conclusion.[150]

The purpose of these advertisements is as straightforward as their appeal to the customer's "bargain" instinct:

Q. Mr. Rabar, what is the basic purpose of Columbia Record Club national advertising?

A. There is only one purpose; to get members.[151]

The sole criteria applied in determining whether a club advertisement will be placed in a particular periodical is whether it produces a "profitable cost per order [member enrollment]" ratio.[152] Every word in the advertisement itself—including the prices quoted, and the artists mentioned by name—is similarly aimed at improving the advertisement's "pull," *i.e.*, the percentage of the advertisement's viewers that respond and join the Club.

In short, this is not "institutional" advertising engaged in to promote these nine competitors' names or their particular "brands":[153] rather, it is straightforward "price" advertising, aimed at selling not so much the idea that these records are "better" than some other sellers' records, but at selling the consumer on the idea that the Columbia Record Club is a better or more economical source from which to buy records the public already knows about. (The Club is normally not interested in offering a record of one of its

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[150] See, *e.g.*, Finding 3, n. 4.

[151] Tr. 6779.

[152] Tr. 5148.

[153] It should be noted that, by and large, the demand for phonograph records runs primarily toward the particular artist, rather than in terms of the "label" of the manufacturer he may happen to be temporarily recording for.

licensors until that record has already become relatively well known, *e.g.*, until its sales hit the 50,000 mark.)

Respondent's argument here is also inconsistent with the relatively short "life" of the typical popular record. There was testimony that the "normal sales curve" of a hit record generally covers a span of some three months (in order to have at least one popular record selling well at any given time, the better known artists carefully arrange to release a new one at least once every three months). In this situation, it is not clear how much "harvest" is actually left in the fields for any newcomers to get from the "old" records advertised by the Club in times past. The real harvest is more likely to come from the sale of records not yet recorded and hence not yet advertised by the Columbia Record Club. The question, then, is not whether some new entrant should be allowed to reap where he never sowed, but whether he should be permitted to participate in *both* the future sowing and the future reaping. We are clear that he should. The Columbia Record Club has, by the admission of its own officials, earned a satisfactory profit on every dollar it has spent so far, including every dollar "invested" in advertising. Having gotten back all that it spent, plus a return it considers satisfactory, we see no rational justification for not allowing new firms to share in whatever profits there may be in the mail order sale of these licensors' *future* records and for denying the record-buying public the benefits of their competition for those profits.

V

Our order is a narrow one, designed simply to stop the fixing of artists' royalties by Columbia and its competitors, and to eliminate the "exclusive" feature of these contracts. In the latter regard, respondents

will be prohibited from entering into or maintaining any contracts with competing record manufacturers that "prevent other club operators, including potential club operators, from acquiring the phonograph records of any other manufacturer or producer on the same terms and conditions as respondents acquire such records. . . ." Elimination of this cost barrier can reasonably be expected to make the club market substantially more attractive to potential entrants and thus to promote the public interest in the development of a more competitive structure and more vigorous competition in this market.

VI

One further matter requires mention here. Respondents and several nonparty witnesses to this proceeding persuaded the examiner to put a mass of data *in camera*. We have examined that material carefully and have found only one exhibit that, in our opinion, ever had any serious claim to being "confidential," and the basis for that claim has been removed by time. This was a *Billboard* market study for 1962.[154] It would of course be improper to unnecessarily publish data that constitutes a firm's stock-in-trade and thus allow its potential customers to get it free rather than having to pay for it. But its saleability was described as depending upon its timeliness, and hence the 1962 data can now have no more "secrecy" value than the 1961 data that was considered already "stale" at the time of the hearings in 1963.[155] The other documents placed *in camera* by the examiner and considered so "confidential" by respondents and these nonparty witnesses consisted largely of sales data and club membership figures. There is nothing "confidential" about

[154] RX 311, *in camera*.
[155] CX 244a, *in camera*.

sales data in an antitrust proceeding; unless it can be used freely, meaningful measurement of the various markets involved are virtually impossible.

Nor is there any presumption of confidentiality for any other data the parties might prefer to call "secret" and withold from public scrutiny. Indeed, the presumption is the other way. Competition depends for its continuing vitality upon free entry and free exit to and from industries, and entry depends in no small measure upon knowledge of opportunities, *i.e.*, knowledge of sales volumes, of probable costs, and of estimated profits. The public interest lies in encouraging entry, not in protecting the barriers erected around industries by established firms, whether these be knowledge barriers or other kinds. Only in the most extraordinary circumstances should data of this kind be withheld from the public record. *H. P. Hood & Sons, Inc.*, 58 F.T.C. 1184 (1961).

An appropriate order will be entered.

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OCTOBER TERM, 1969

No. 853

FEDERAL TRADE COMMISSION,
Petitioner,

v.

COLUMBIA BROADCASTING SYSTEM, INC. and COLUMBIA RECORD CLUB, INC.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI

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January 16, 1970

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